Supreme Court, U.S.
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NO. _____

IN THE

Supreme Court of the United States

TIME WARNER ENTERTAINMENT COMPANY, L.P., *et al.*,
Petitioners,

v.

FEDERAL COMMUNICATIONS COMMISSION AND
UNITED STATES OF AMERICA,
Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

PETITION FOR A WRIT OF CERTIORARI

FERNANDO BOHORQUEZ, JR.
ANGELA J. CAMPBELL
INSTITUTE FOR PUBLIC REPRESENTATION,
GEORGETOWN UNIVERSITY LAW CENTER
600 New Jersey Ave., NW
Suite 312
Washington, D.C. 20001
(202) 662-9535

ANDREW JAY SCHWARTZMAN
(Counsel of Record)
CHERYL A. LEANZA
HAROLD J. FELD
MEDIA ACCESS PROJECT
950 18TH ST., SUITE 220
Washington, D.C. 20006
(202) 232-4300

Counsel for Consumer Federation of America, et al.

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QUESTIONS PRESENTED

In the ruling below, the United States Court of Appeals for the District of Columbia Circuit set aside a regulation of the Federal Communications Commission on both statutory and First Amendment grounds. The FCC rule implemented a facially-constitutional 1992 Cable Act directive that the Commission adopt a national cable ownership limit in order to foster diversity of cable programming and prevent industry concentration. After a notice and comment rulemaking, the FCC adopted a nationwide limit of 30%. The D.C. Circuit's ruling setting aside this limit opened the door to further concentration in the cable industry, an industry in which the three largest actors already control about half of the market. Moreover, the ruling has triggered a spate of litigation seeking to overturn ownership rules in a variety of other media subject to FCC regulation. The questions presented for review are:

1. Whether the FCC's 30% regulation (1) was justifiable based on the 1992 Act's objective of promoting diversity and (2) was adequately supported by a record comprised of detailed Congressional and agency findings?

2. Whether the First Amendment limits the FCC's ability to set a ceiling on the number of subscribers any one cable operator may reach in order to achieve the constitutionally-valid congressional goals of diversity and competition?

RULE 14.1(b) STATEMENT

The parties in the United States Court of Appeals for the District of Columbia Circuit, Docket No. 94-1035, were Time Warner Entertainment Co., L.P ("Time Warner"), as Petitioner, and the Federal Communications Commission and the United States ("FCC, *et al.*") as Respondents. Intervenors were Bell South Telecommunications, Inc.; Bell Atlantic Telephone Companies; AT&T Corporation; and Consumer Federation of America , Center for Media Education, Association of Independent Video and Filmmakers, National Association of Artists, National Alliance for Media Arts and Culture, Office of Communication of the United Church of Christ, Inc., and National Council of Senior Citizens (collectively "CFA, *et al.*").

Parties to Docket No. 95-1337, consolidated in 94-1035, were Time Warner, Petitioners and FCC *et al.*, Respondents. Intervenors were Cox Communications, Inc., Bell Atlantic Telephone Co., and U.S. West, Inc.

Parties to Docket No. 99-1503, consolidated in 94-1035, were Time Warner, Petitioners, and FCC, *et al.*, Respondents. Petitioner-Intervenor was AT&T Corp. Intervenors were CFA, *et al.*

Parties to Docket No. 99-1504, consolidated in 94-1035, were Time Warner, Petitioners, and FCC, *et al.*, Respondents. Intervenors were AT&T Corp. and CFA, *et al.*

Parties to Docket No. 99-1522, consolidated in 94-1035, were Petitioners Consumers Union and Respondents FCC, *et al.* Intervenors were Time Warner and AT&T Corp.

Parties to Docket No. 99-1541, consolidated in 94-1035, were Petitioners AT&T Corp. and Respondents FCC, *et al.* Intervenor was Time Warner.

Parties to Docket No. 99-1542, consolidated in 94-1035, were AT&T, Petitioners and FCC, *et al.*, Respondents. Intervenor was Time Warner.

Parties to Docket No. 00-1086, consolidated in 94-1035, were Petitioners Consumers Union and Respondents FCC, *et al.*

RULE STATEMENT 29.6

Consumer Federation of America, Consumers Union, Center for Media Education, Association of Independent Video and Filmmakers, National Association of Artists, National Alliance for Media Arts and Culture, Office of Communication of the United Church of Christ, Inc., and National Council of Senior Citizens have no parent companies, subsidiaries, or affiliates that have issued shares to the public.

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PETITION FOR A WRIT OF CERTIORARI

Petitioners, Consumer Federation of America, Consumers Union, Center for Media Education, Association of Independent Video and Filmmakers, National Association of Artists, National Alliance for Media Arts and Culture, Office of Communication of the United Church of Christ, Inc., and National Council of Senior Citizens respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the District of Columbia Circuit in this case.

OPINIONS BELOW

The opinion for the United States Court of Appeals for the District of Columbia Circuit is reported at 240 F.3rd 1126 (App. 1-29).[1] The order of the United States Court of Appeals for the District of Columbia Circuit denying the Petition for Rehearing is unpublished (App. 30-31). Decisions of the Federal Communication Commission in MM Docket No. 92-264, Implementing Sections 11 and 13 of the Cable Television Consumer Protection and Competition Act of 1992, the Horizontal and Vertical Ownership Limits, are reported as follows: *Second Report and Order and Further Notice of Proposed Rulemaking* is reported at 8 FCC Rcd 8565 (App. 53-96); the *Memorandum Opinion and Order, Order on Reconsideration and Further Notice of Proposed Rulemaking* is reported at 13 FCC Rcd 14462 (App. 115-180); and *Third Report and Order* is reported at 14 FCC Rcd 19098 (App. 254-311).

JURISDICTION

The judgment of the Court of Appeals was entered on March 2, 2001 (App. 1-29). A timely petition for rehearing was denied on May 4, 2001 (App. 30-31). The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

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[1] "App." refers to the separately bound appendix.

CONSTITUTIONAL, STATUTORY AND REGULATORY PROVISIONS INVOLVED

First Amendment, United States Constitution:
Congress shall make no law respecting ... abridging the freedom of speech, or of the press ....

Section 11(c) of the 1992 Cable Television Consumer Protection and Competition Act, as codified in 47 USC §533(f)(1-2):
§533. Ownership restrictions

* * * *

(f)(1) In order to enhance effective competition, the Commission shall, within one year after the date of enactment of the Cable Television Consumer Protection and Competition Act of 1992 (enacted Oct. 5, 1992), conduct a proceeding -

(A) to prescribe rules and regulations establishing reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such person or in which such person has an attributable interest....

* * * *

(2) In prescribing rules and regulations under paragraph (1), the Commission shall, among other public interest objectives -

(A) ensure that no cable operator or group of cable operators can unfairly impede, either because of the size of any individual operator or because of joint actions by a group of operators of sufficient size, the flow of video programming from video programmer to the consumer;

(B) ensure that cable operators affiliated with video programmers do not favor such programmers in determining carriage on their cable systems or do not favor such programmers in determining carriage on their cable systems or do not unreasonably restrict the flow of video programming of such programmers to other video distributors;

(C) take particular account of the market structure, owner-

ship patterns, and other relationships of the cable television industry, including the nature and market power of the local franchise, the joint ownership of cable systems and video programmers, and the various types of non-equity controlling interests;

(D) account for any efficiencies and other benefits that might be gained through increased ownership or control;

(E) make such rules and regulations that reflect the dynamic nature of the communications marketplace;

(F) not impose limitations which would bar cable operators from serving previously unserved rural areas; and

(G) not impose limitations which would impair the development of diverse and high quality video programming.

47 C.F.R. §76.503:

§ 76.503 National subscriber limits.

(a) Subject to paragraph (b) of this section, no cable operator shall serve more than 30% of all multichannel-video programming subscribers nationwide through multichannel video programming distributors owned by such operator or in which such cable operator holds an attributable interest.

(b) Cable subscribers that a cable operator does not serve through incumbent cable franchises shall be excluded from the cable operator's limit.

(c) For purposes of this section, "incumbent cable franchise" means a cable franchise in existence as of October 20, 1999 and all successors in interest to these franchises.

(d) Subscribers that a cable operator serves through incumbent cable franchises shall include all subscribers served by those incumbent cable franchises, regardless of when the subscribers were added to the incumbent cable franchise system.

(e) "Multichannel video-programming subscribers" means subscribers who receive multichannel video-programming from cable systems, direct broadcast satellite services, direct-to-

home satellite services, multichannel multipoint distribution services, local multipoint distribution services, satellite master antenna television services (as defined in § 76.5(a)(2)), and open video systems.

(f) "Cable operator" means any person or entity that owns or has an attributable interest in an incumbent cable franchise.

(g) Prior to acquiring additional multichannel video-programming providers, any cable operator that serves 20% or more of multichannel video-programming subscribers nationwide shall certify to the Commission, concurrent with its applications to the Commission for transfer of licenses at issue in the acquisition, that no violation of the national subscriber limits prescribed in this section will occur as a result of such acquisition.

STATEMENT

This petition seeks review of a decision of the D.C. Circuit that opens the door to substantial consolidation and restructuring in the cable industry in contradiction to the express desire of Congress. This decision creates precedent for overturning a significant portion of other FCC media ownership rules.

A. Facts Leading to the Passage of the 1992 Cable Act.

In 1989, Congress began a three-year investigation into the cable television industry, resulting in its sweeping re-regulation. Cable Television Consumer Protection and Competition Act of 1992, Pub. L. 102-835, 106 Stat. 1460 ("1992 Cable Act").

Undergirding the 1992 Cable Act is a deep and searching legislative history of over 12,000 pages documenting Congress' alarm at the cable industry's consolidation.

"Horizontal concentration was increasing as a small number of multiple system operators (MSO's) acquired large numbers of cable systems nationwide. .... The trend was accelerating, giving the MSO's increasing market power. ***In 1985, the 10 largest MSO's controlled cable systems service slightly less than 42 percent of all cable subscribers; by 1989, the figure was***

nearly 54 percent. *Turner Broad. Sys., Inc. v. FCC*, 520 U.S. 180, 197 (1997) (citations omitted) (emphasis added) ("*Turner II*"). In "unusually detailed" legislative findings, *Turner Broad. Sys., Inc. v. FCC*, 512 U.S. 622 at 646 (1994) ("*Turner I*"), Congress concluded:

> The cable industry has become highly concentrated. The potential effects of such concentration are barriers to entry for new programmers and a reduction in the number of media voices available to consumers.

1992 Cable Act, §2(a)(4). It determined that national policy was to:

> [P]romote the availability to the public of a diversity of views and information through cable television and other video distribution media.

1992 Cable Act, §2(b)(1); *see also id.* §2(a)(6).

Members specifically considered the implications of consolidation and the adequacy of antitrust laws to address it:

> Federal policy has always been vigilant to restrain concentration when it threatened diversity of voices *even though it did not rise to the level of an anti-trust violation.*

S.Rep. No. 102-92, at 32-33 (1991) (emphasis added) ("S.Rep.").

Congress studied the national market for programming acquisition, finding that it was rapidly becoming vertically integrated with the cable operators' distribution networks. 1992 Cable Act, §2(a)(5). Operators would "force programmer[s] to buy their way onto cable by giving up an equity interest in their programming." S.Rep. at 24.

Not only did individual operators purchase and invest in individual programming services, but multiple operators often simultaneously invested in programmers. Through their investments, major operators that might have otherwise competed in programming acquisition developed a web of alliances

with each other, minimizing their rivalries and reducing opportunities for a competing channel to gain carriage from any operator. *Media Ownership: Diversity and Concentration, Hearings Before the Subcomm. on Communications of the Comm. on the Senate Commerce, Science, and Trans.*, S.Hrg. 101-357, at 379-85 (1989) ("S.Hrg. 101-357").[2] In one infamous example, a large number of cable operators–all with a stake in the Cable News Network–denied carriage to NBC's proposed news channel, CNBC, unless it agreed to circumscribe its coverage in a manner the FCC concluded was likely "to protect CNN from competition." *Id.* at 301, 609-10; *Competition, Rate Deregulation and the Commission's Policies Relating to the Provision of Cable Television Service, Report*, 5 FCC Rcd 4962, 5028-29 (1990)

Cable operators controlled the subscribers a new programming channel needed to succeed, and thus "ha[d] the market power to determine what programming services can 'make it' on cable." S.Rep. at 33. Successfully launching a channel was not easy. [3]

Cable operators denied their competitors, such as DBS operators, access to popular programming they needed to win customers. S.Rep. at 26. Even independently owned channels agreed to exclusive agreements with cable operators to avoid angering their largest customers. *See Hearings on S. 1880, Before*

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[2]For example, TCI jointly invested in various programmers with Time, Storer Cable Communications, Cablevision, and Comcast, and some of those operators also jointly invested in other programmers. *Id.*

[3]For example, the President of Discovery Network explained how, in 1982-83, he conceived of a new documentary channel, mortgaged his house, and sought for 18 months to raise the necessary $20 million in capital to launch a programming service that would not reach the minimum number of subscribers necessary to become self-supporting for one to two years. S. Hrg. 101-357, at 217-19. Only through a last-minute cooperative investment by several cable operators did the channel stave off bankruptcy. *Id.*

the Subcomm. on Communications of the Senate Comm. on Commerce, Science, and Trans., S. Hrg. 101-702, at 273, 412-13 (1990); S.Hrg. 101-357, at 345-48.

Consequently, Congress directed the Federal Communications Commission ("Commission" or "FCC") to adopt a prophylactic national cap to prevent growth of individual cable operators beyond "reasonable limits." 1992 Cable Act, §11(c). Section 11(c) contains two main subsections. The first subsection directs the Commission to conduct a proceeding to prescribe rules, and begins with the phrase "[i]n order to enhance effective competition." 47 U.S.C. §533(f)(1). The second states the FCC "shall, among other public interest objectives," take into account seven factors, including factors that specifically address the diversity of programming consumers receive. 47 U.S.C. §§ 533(f)(2)(A), (B), (C), (G).

B. Current State of the Cable Industry.

The cable industry's horizontal and vertical consolidation has continued unabated since Congress' findings in 1992. For example, in 1997, the Federal Trade Commission ("FTC") concluded that the cable television programing market is highly concentrated. *Time Warner Inc., Turner Broad. Sys. Inc., Telecommunications Inc., and Liberty Media Corp.*, FTC Docket No. C-3709, Complaint, ¶30, 1997 WL 65377 (Feb. 3, 1997). It further concluded that entry into the programming market is "difficult," taking "more than two years to develop [a service] to a point where it has a substantial subscriber base and competes with ... 'marquee' ... service[s]" *Id.* ¶34.

By 2000, the top ten cable operators added 30 points to the national subscriber share they held in 1992, increasing the figure to 84%, and reflecting a sharp increase from 1999, when it was 75%. *Seventh Annual Video Programming Competition Report*, FCC 01-01, CS Docket 00-132, ¶171 (Jan. 8, 2001). The top three cable operators control 47% of the market. *Id.* at Table

C-3. FCC cable industry data demonstrate the impact of the 30% limit in the present market. Without the rule, concentration rises to a level that Department of Justice ("DOJ") antitrust standards classify as highly concentrated.[4] Moreover, multiple cable operators continue to jointly invest programming channels with the highest proportion of subscribers. *Id.* at Tables D-6, D-7.[5] Non-affiliated programmers' dependence on the largest cable operators continues as well. General Accounting Office, GAO/RCED-99-158, *The Changing Status of Competition to Cable Television*, at 22 (1999).

C. Proceedings Below.

1. FCC Decisions.

The FCC established a 30% horizontal ownership limit in 1993,[6] App. 66, it further developed its record and analysis in 1998, App. 115-80, and 1999. App. 254-311.

The FCC concluded that Section 11(c) was adopted because "Congress was concerned in particular with preventing large vertically integrated cable systems from creating barriers to entry for new video programmers, and from causing a reduction in the number of media voices available to consumers." App. 58. It found that Congress was concerned about cable

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[4]The DOJ's measures market concentration by the Herfindahl-Hirschman Index ("HHI). DOJ considers an HHI between 1000 and 1800 to be moderately concentrated, and above 1800 to be highly concentrated. *Id.* at n.572. According to FCC data, the cable programming market's current HHI is 1814. *Id.* at Table C-3. If AT&T completes the suspended divestiture required by the ownership rule described *infra* at n. 12, the HHI will be reduced to 1118.

[5]This data shows 9 of the top 20 channels by subscribership and 11 of the top 20 channels by prime time ratings are vertically integrated, of those, 7 maintain joint investments from two operators.

[6]The Commission adopted this limit in 1993, but immediately stayed it when the underlying statute was declared unconstitutional, as explained *infra* at note 9. App. 54.

operators' ability to exercise monopsony power in the program acquisition market and that "[a]lthough under traditional antitrust analysis the cable industry is relatively unconcentrated, the 1992 Cable Act requires the Commission to establish limits on horizontal concentration." *Id.*

The FCC described the trend toward larger cable operators and received extensive comment from members of the cable industry describing their desire to expand. *See, e.g., id.* at 272-73, 277, 281, 285. The FCC found that the "market power of large cable operators has the potential to prevent nascent cable networks from even launching and to cause current networks to fail." *Id.* at 291.

Utilizing detailed economic studies of the cable industry, data submitted to the FCC by cable operators, its own reviews of the industry, and antitrust analysis, *see, e.g, id.* at 291-297, it concluded that new programming services need access to 40% of the nation's TV homes to attain viability.[7] *Id.* at 161-67, 278-300.[8] The Commission considered the impact of limits at 20, 30, and 40 %, considering the number of competitors each limit would likely produce. App. 62-65, 320-22, 161-62; 258. 284, 288-293. Reviewing the range of limits, it concluded a 30% limit would make it more difficult for them to "act in concert" in program purchasing because "reaching consensus, monitoring compliance, and punishing cheaters" would be more difficult. *Id.* at 138-40. It looked at the consequences of duopolies of equal or unequal size, and of more than two competitors. *Id.*

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[7]The FCC conducts its analysis on homes with televisions, called "television households." *Id.* at 322-31.

[8]The FCC based this estimate on a detailed review indicating that a new programmer needs to reach about 15 million subscribers, or an estimated 20% of the market, to ensure viability, App. 282-83, and that the programmer has a 50% chance of obtaining subscribers. *Id.* at 287; *see also id.* at 7-8.

Ultimately, the Commission reasoned that a 30% limit would balance between its costs and benefits, App. 125-126, and would best ensure the availability of the market to new programming services because a 30% limit would "ensur[e] ... at least 4 [operators] in the marketplace" and "will prevent two large operators from obtaining control over [more than] 60% of the market," *id.* at 290, and produce a "greater variety of media voices ... available to the public." *Id.*

The FCC also observed that, even under existing ownership limits, "credible evidence" indicated the largest operators could induce programmers not to sell their programming to competitors. *Id.* at 295; *see also id.* at 207-09. The FCC rejected claims that the cap should be based on a concern for unilateral action alone, however, citing the statutory concern with joint action. *Id.* at 284.

2. D.C. Circuit Decisions.

Last year, in the face of a First Amendment challenge, a panel of the D.C. Circuit declared that §11(c) of the 1992 Act is facially constitutional.[9] *Time Warner Entm't Co. v. United States*, 211 F.3d 1313 (D.C. Cir. 2000), *cert. den.*, 121 S. Ct. 1167 (2000) (*"Time Warner I"*). The court determined that Congress reviewed evidence showing that the increasing consolidation of the cable industry limited the likely success of new, independ-

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[9]More than eight years elapsed before the court considered the validity of the FCC's rules. Time Warner and other cable operators challenged the constitutionality of §11(c) on its face immediately in 1993 and a lower court invalidated the horizontal ownership limit that year. *Daniels Cablevision, Inc. v. United States*, 835 F. Supp. 1 (D.D.C. 1993). Time Warner subsequently filed a petition for review of the FCC's rules, which the D.C. Circuit later consolidated with the appeal of the statutory challenges. *Time Warner v. FCC*, 93 F.3d 975, 979-80 (D.C. Cir. 1996). In 1999, because the FCC continued to revise its rules, the court re-severed the two cases, considering the constitutionality of the statute separately from the rules. *Id.* at 1315-16.

ent programmers. It found that "Congress reasonably concluded that this concentration threatened the diversity of information available to the public and could form a barrier to the entry of new cable programmers. That is hardly an unreasonable inference." *Id.* at 1320.

On March 2, 2001, another panel of the D.C. Circuit vacated the FCC's rules, in an opinion authored by Judge Williams. App. 1-29. Despite the extremely detailed legislative and agency findings, the court found that the FCC had not met its burden under the First Amendment and lacked statutory authority for some of its actions. *Id.* at 2.

The court did not contest the FCC's conclusion that a new programmer needs an "open field" of 40%, *id.* at 9, but concluded that the FCC's analysis supported a rule limiting cable operators to 60%, rather than 30%, of subscribers. *Id.*

Although the court concluded that statutory authority to protect programmers from the action of one operator "flows plainly" to the FCC because "if the [government's interest] in diversity is to mean anything ... the government must be able to ensure that a programmer have at least two conduits through which it can reach the number of viewers needed for viability," *id.* at 8, the court did not extend its deference to Congress' language addressing multiple operators. The court concluded that the FCC must make a separate, and more significant, showing to justify a limit that protects potential programmers from joint cable operator action. *Id.*

Specifically, the court believed that a lower, 30% cap could be justified only if: (1) there was a non-conjectural risk that two or more operators would "collude" to deny carriage to a programmer, or (2) the FCC had the authority under the 1992 Act to promote diversity by regulating the unilateral acts of cable operators. App. 9.

The court's analysis of the first issue hinged on one of the

many terms used by the FCC to consider the cap–the term "collusion." The court concluded that either Congress or the FCC must produce "substantial evidence" of "collusion" to meet the *Turner I* and *Turner II* standard. *Id.* at 9. The court found fault with Congress for failing to identify "collusion" specifically. *Id.* It found that the language Congress did use was inadequate, concluding that the statutory language "authorizing regulations to protect against '*joint* actions by a group of operators of sufficient size,'" was not a finding of "probable" collusion but instead evidenced only a *"possibility"* of collusion. *Id.* at 9 (quoting §533(f)(2)(A) (court's emphasis)).

The court then determined that the FCC also had not produced a sufficient record through its own proceedings. App. 10-11. The court dismissed as "economic commonplace" the Commission's analysis concluding that a limit producing three large competitors instead of two large competitors was preferable because collusion is less likely when there are more firms. *Id.* at 10.

With respect to the second issue, the court sharply limited the Commission's ability to adopt regulations based on diversity, as opposed to competitive concerns. The court concluded that the first of seven guideposts in Section (f)(2) was the "relevant provision." App. 14-15. This section directed the FCC to ensure that no cable operator or group of operators could "unfairly impede ... the flow of video programming to the consumer." 47 U.S.C. §533(f)(2)(A). The court acknowledged the term "unfair" was "extremely vague." *Id.* at 15. The court also acknowledged that Section 11(c) contains the "duality" of competition and diversity which run throughout the 1992 Cable Act. *Id.* at 15-16. Nonetheless, the court determined the introductory phrase in §533(f)(1)("to enhance effective competition") was plain enough for it to conclude that Congress' "primary" goal was to promote "fair"–meaning "eco-

nomic"-competition. *Id.* at 15.

The court therefore rejected the Commission's interpretation of the statute based on the Act's codified legislative findings. App. 16-17. It did not address subsection (f)(2)'s remaining diversity directives. *Id.* As a result, the court held that the FCC could not achieve its goal of preserving a multiplicity of programming sources by selecting an ownership limit lower than that necessary to achieve fair competition alone. *Id.* at 14.

REASONS FOR GRANTING THE WRIT

I. THE INSTANT CASE WARRANTS REVIEW BECAUSE ITS FLAWED CONSTITUTIONAL DOCTRINE WOULD THREATEN NEARLY EVERY FCC MEDIA OWNERSHIP REGULATION.

Any decision invalidating, on constitutional grounds, a federal agency's implementation of a concededly valid statutory directive to impose industry-wide ownership limits is surely a matter of importance.[10]

Certiorari is especially appropriate here, not just because of the decision's intrinsic jurisprudential importance, but also because this case involves the mechanisms of citizenship. As this Court has emphasized, "assuring that the public has access to a multiplicity of information sources is a governmental purpose of the highest order, for it promotes values central to the First Amendment." *Turner I*, 512 U.S. at 663.

The precedential force of the D.C. Circuit's opinion promises to bring immediate and sweeping changes to ownership concentration in ***all*** electronic media industries.

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[10]Because the D.C. Circuit has exclusive jurisdiction of many telecommunications cases, *see* 47 U.S.C. §402(a), and is the traditional venue for most other broadcast and cable cases, it is highly unlikely that other circuits will consider the issues presented here. Thus, there is no reason for this Court to await the development of inter-circuit conflicts before granting certiorari.

This is ***not*** a matter of speculation: the court's decision has ***already*** been extended to justify interim relief suspending FCC rules limiting national and local broadcast station ownership, and it has been employed to challenge the Commission's ban on TV/cable cross-ownership rules. The immediate effect of this case was so dramatic that it became the subject of a page one *New York Times* story. Evaluating the impact of this case and the Viacom stay discussed below, the *Times* said that "[i]n a marked departure from decades of Supreme Court opinions on the subject, the appeals court and the FCC have become significantly ... more skeptical of the role of government in promoting diversity in mass media." "Media Companies Succeed in Easing Ownership Limits," *New York Times*, p. 1, April 16, 2001.

AT&T/Time Warner Divestiture - Just two weeks after the panel issued its decision, without awaiting issuance of the Circuit's mandate, the FCC, *sua sponte*, cited this case in relieving Respondent AT&T Corp. (the largest cable operator) of a May 19, 2001 deadline to divest its 22.5% partnership interest in the second largest cable operator, Respondent Time Warner Entertainment. *MediaOne Group, Inc.*, 16 FCC Rcd 5835 (2000). Thus, as a direct consequence of this case, AT&T now has ownership interests in cable systems reaching almost 40% of the nation's TV homes.[11]

Proposed Sale of AT&T Cable - In the weeks preceeding submission of this petition, Comcast, (the third largest operator) and AOL/Time Warner (the second largest) have publicly disclosed that each has been negotiating a possible takeover of AT&T. Industry executives, financial analysts, and press

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[11] *Letter from Douglas G. Garrett*, Docket 99-251 (filed June 29, 2001). When Congress mandated the cable ownership cap in 1992, the largest operator had a 25% share of that market. H.R. Rep. No. 102-628, at 42 (1992).

commentators pointed to the decision below when predicting that such combinations (which might result in a single operator serving well over half the nation's cable subscribers) could receive FCC approval.[12]

National Broadcast Ownership - The impact of the decision has not been limited to cable operators. On April 6, 2001, the D.C. Circuit granted a stay excusing Viacom, Inc. from complying with an FCC directive to divest one or more television stations to come into compliance with the FCC's 35% national ownership limit on broadcast properties. *Viacom, Inc. v. FCC*, No. 01-1136 (D.C. Cir., April 6, 2001).[13] Because of the *Viacom* stay, the FCC has indefinitely deferred enforcement of a similar requirement as applied to News Corp., the parent of the Fox network.[14] The FCC Chairman has publicly stated his doubt as

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[12]*See, e.g.*, "Regulatory Forecast Looks Fair for Possible Comcast Corp./ AT&T Broadband Merger," *Multichannel News*, p. 5, July 16, 2001; "Experts Say Regulators Would Likely Approve Comcast, AT&T Merger," *The Philadelphia Inquirer*, July 14, 2001 (referring to the court's decision as giving Comcast "an especially good time to bid because the old ownership rules were not in force...."); "Deal Should Face Little Opposition from Regulators," *The Wall Street Journal*, p. B1, July 10, 2001 ("But ownership caps were overturned by a federal appeals court earlier this year, and the FCC has yet to replace them. That means cable companies are enjoying a rare regulatory free-for-all.").

[13]The Appellants' March 19, 2001 *Emergency Motion for Interim Relief* argued that *Time Warner v. FCC* was controlling precedent. *See also CBS Corporation*, FCC No. 01-94 (March 16, 2001) (denying application for stay) ("I believe the facts before the Commission and the recent *TWE* decision warrant the interim relief sought by Viacom.")(Furchgott-Roth, dissenting). The case was brought under 42 U.S.C. §402(a), which, as is noted in note 10, *supra*, confers exclusive jurisdiction on the D.C. Circuit.

[14]*See UTV of San Francisco Inc.*, FCC No. 01-201 (rel. July 25, 2001) ("In light of [the *Viacom* stay], we believe it is appropriate to delay the effectiveness of our condition requiring [Fox] to come into compliance ... Accordingly, [Fox] will be afforded a period of 12 months following entry of a final deci-

to whether the national broadcast ownership cap will withstand review under the precedent of this case.[15]

Local Broadcast Ownership - The decision was also the basis for a successful motion for stay of the required divestiture of four TV stations under the Commission's local television duopoly rules. *Sinclair Broadcast Group v. FCC*, No. 01-1079 (D.C Cir. June 20, 2001). It has been reported that the FCC "is reviewing whether to extend the delay to ... other [broadcast ownership] groups" and that the several companies under similar divestiture orders "are likely to get some relief ... pending the outcome of a court challenge ...." *Broadcasting and Cable*, July 2, 2001, p. 4.

Local Cable/Broadcast Cross-Ownership - Time Warner has also sought to extend the precedent of this case to the FCC's rule prohibiting common ownership of TV stations and cable systems in the same market. Its June 15, 2001 brief to the D.C. Circuit in Docket No. 00-1222 cites this case as the principal authority on which its challenge is based.

This decision must be reviewed now because the ownership consolidation it invites cannot be unraveled. After transactions are consummated, "it becomes difficult, and sometimes virtually impossible, to 'unscramble the the eggs.'" *Consolidated Gold Fields PLC v. Minorco, .A.*, 871 F.2d 252, 261 (2d Cir.), *amended*, 890 F.2d 569 (2d Cir.), *cert. dismissed*, 492 U.S. 939 (1989) (*quoting*

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sion... upholding the national broadcast ownership cap. "). Judicial review of this decision would, under 42 U.S.C. §402(a), occur in the D.C. Circuit.

[15]In an interview transcript posted on the Chairman's personal web page, he speculated that "Many people see [the stay] as a grave sign for the life of the rule....[N]ot so many weeks ago the court struck down horizontal rules in the cable context - potentially signaling sort of similar skepticism about this rule....[The court] has made already some judgment that there is a likelihood to prevail on the merits of the petition." *Conversation With Sam Donaldson*, www.fcc.gov/Speeches/Powell/2001/spmkp102.pdf (accessed July 26, 2001).

Sonesta Int'l Hotels Corp. v. Wellington Assocs., 483 F.2d 247, 250 (2d Cir. 1973)). The problem is worse when consolidation removes "an effective competitor in markets of vital interest to the nation's economy...." *Grumman Corp. v. LTV Corp.*, 665 F.2d 10, 16 (2d Cir. 1981)).

II. THE COURT VIOLATED BASIC PRINCIPLES OF STATUTORY CONSTRUCTION AND DID NOT APPROPRIATELY DEFER TO THE AGENCY'S REASONABLE CONSTRUCTION OF THE ACT.

Only the D.C. Circuit's misinterpretation of the 1992 Cable Act allowed it to reach the First Amendment issues in this case. The panel sharply departed from the "elementary rule ... that every reasonable construction must be resorted to, in order to save a statute from unconstitutionality." *INS v. Enrico St. Cyr.*, 121 S. Ct. 2271, 2279 n. 12 (2001) (quoting Hooper *v. California*, 155 U.S. 648, 657 (1895)); *Edward J. DeBartolo Corp. v. Florida Gulf Coast Bldg. & Constr. Trades Council*, 485 U.S. 568, 575 (1988) ("*DeBartolo*")(applied to agency's construction of a statute).

In previously upholding the facial constitutionality of §11(c), the *Time Warner I* court held that the concentrated cable industry posed a real, non-conjectural harm to diversity. 211 F.3d at 1320. Notwithstanding this holding, the court removed "diversity" from the First Amendment calculus when it declared the rules unconstitutional.

After finding that the FCC lacked the authority to limit ownership based on diversity, the court was free to narrow the First Amendment question as to whether Congress or the FCC had provided substantial evidence that two or more operators would "collude" to deny carriage to a programmer. App. 7. As a result, as detailed in Part I *supra*, the very dangers Congress foresaw and sought to prevent are now rapidly coming to pass.

A. The Court Improperly Construed the Statute to Exclude Diversity.

The Panel concluded that the FCC lacked statutory authority to limit the size of cable operators based on diversity concerns, and, in stark conflict with the statutory language, must instead act only on the court's notions of antitrust law. The opinion below disregarded the plain language of 11(c), failed to consider the statutory context, and brushed aside the mutually reinforcing nature of diversity and competition.

The panel erred in failing to read Section 11(c) within the statutory context of the 1992 Cable Act and the 1934 Communications Act. Basic canons of statutory construction require interpretation of this language and the purpose in the context of the statute as a whole. *FDA v. Brown & Williamson Tobacco*, 529 U.S. 120, 132-33 (2000). In particular, where Congress chooses to amend the Communications Act rather than enact a freestanding provision, the court must read the separate statutory provisions in light of the broad purposes and powers of the Communications Act as a whole. *AT&T v. Iowa Utilities Bd.*, 525 U.S. 366, 377-78 (1999).

Section 533(f)(2) directs that in setting ownership limits, the FCC "shall" consider "other public interest objectives." This Court has consistently construed the term "public interest" as embodying diversity. *National Broadcasting Co. v. United States*, 319 U.S. 190, 226 (1943). As this Court has explained, "the 'public interest' standard necessarily invites reference to First Amendment principles," and, in particular, to the First Amendment goal of achieving "the widest possible dissemination of information from diverse and antagonistic sources." *FCC v. NCCB*, 436 U.S. 775, 795 (1978) (citations omitted).[16]

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[16]The concern with diversity does not conflict with the statute's stated purpose of "enhanc[ing] effective competition." §533(f)(1). To the contrary,

Four other public interest factors listed in §533(f)(2) explicitly refer to Congress' objective of promoting diversity. As the Commission emphasized, "[Sections 533(f)(2)(A), (B), (C) and (G)] require the Commission to ensure that operators, unilaterally or in coordination, do not unreasonably restrict the flow of video programming to consumers and do not hinder the development of new programing from diverse voices." App. 280.

In contrast, relying on the term "unfair" in §533(f)(2)(A), the panel concluded that the statute addressed only two situations - a single cable operator's actions, or, the "collusive" behavior of several operators. App. 6. The panel reached this result by relying on the introductory phrase of (f)(1), concluding "that *these* regulations are to be promulgated '[i]n order to enhance effective competition.'" App. at 16 (emphasis original).[17] The panel therefore dismissed the FCC's reliance on the congressional finding that the "'cable industry has become highly concen-

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"our past decisions have recognized, moreover, that the First Amendment ***and*** antitrust values underlying the Commission's diversification policy may properly be considered by the Commission in determining where the public interest lies." *NCCB*, 436 U.S. at 795(emphasis added). *See also Turner II*, 520 U.S. at 198.

[17]In attempting to read the statute as a limitation on the FCC's discretion, the court compared the purposes of §533(f) to two other sections of the 1992 Act which also contain specific directives for implementation. App. 16, n.8. Actually, all three sections explicitly expand the FCC's powers. However, were it true that the purposes set out in those two sections did limit the FCC's discretion, that is indubitably not the case for §533(f); unlike the other provisions, this one gives the FCC a range of objectives, from which it must pick and choose. *See FCC v. WNCN Listeners Guild*, 450 U.S. 568, 596 (1981) ("[D]iversity is not the only policy the Commission must consider....[Its] implementation ... when based on a rational weighing of policies ... is not to be set aside."); *Northeast Utilities Service Co. v. FERC*, 993 F.2d 937, 952-53 (1st Cir. 1993)(agency discretion is at its "zenith" when balancing among objectives).

trated,'" 1992 Cable Act §2(a)(4), and the general policy of promoting diversity, §2(b)(1). App. 16. The Panel concluded that "reference to a Congressional finding cannot overcome clear language and purpose of the actual provision." *Id.*

While a finding may not override statutory language, it does inform interpretation of the word Congress did use, "unfairly," particularly when, as the Panel admits, that word is "extremely vague." *Id.* at 15. Given the FCC's broad powers under the Communications Act to promote diversity ***and*** competition, *NCCB*, 436 U.S. at 798-802, the court should not have interpreted either "unfairly" or "enhance effective competition" as constricting the FCC's authority to regulate based on diversity concerns. *See, e.g., Whitman v. Am. Trucking Ass'n, Inc.*, 121 S. Ct. 903, 910 (2001) (Congress "does not ... hide elephants in mouseholes"); *see also United States v. Storer Broadcasting* Co., 351 U.S. 192, 203 (1956); *Oceanair of Fla,, Inc. v. U.S. Dep't. of Transp.*, 876 F.2d 1560, 1564 (11th Cir. 1989) ("[C]ourts should not infer that Congress intended to restrict an agency's broad powers ... unless Congress has explicitly done so.").

The court below improperly used the surrounding words in the statute to substitute its own strict re-reading of a single statutory word for the agency's reasonable construction and in violation of the plain language. *Babbit v. Sweet Home Chapter of Communities for a Greater Ore*, 515 U.S. 687, 708 (1995)("*Sweet Home*").; *FTC v. Mandel Bros., Inc.*, 359 U.S. 385, 389-390 (1959). This renders "mere surplusage," *Sweet Home*, 515 U.S. at 698, the phrase "among other public interest objectives" and the remaining factors Congress enumerated for the FCC to consider. Such judicial revisionism is "an undertaking more consonant with the task of a congressional committee than with judicial construction." *Mandel Bros.*, 359 U.S. at 390. Indeed, by redrafting the statute in this fashion, the panel opened the door to the very consolidation §11(c) sought to prevent.

B. The Panel Failed to Defer to the Agency And Thus Unnecessarily Created a Constitutional Conflict.

The Panel's refusal to defer did more than misapply the relevant standard. It created an unnecessary Constitutional conflict, striking down the regulations on First Amendment grounds. In such a case, a construction that defers to the agency is particularly warranted. *DeBartolo*, 485 U.S. at 575.[18]

This Court has consistently recognized that "[w]hen Congress has explicitly left a gap for an agency to fill, there is an express delegation of authority to elucidate a specific provision of the statute by regulation." *United States v. Mead Corp.*, 121 S.Ct. 2164, 2170 (2001) (quoting *Chevron.*, 467 U.S. 837, 843-844 (1984)). "[A] court may not substitute its own construction of a statutory provision for a reasonable interpretation made by ... an agency." *Chevron*, 467 U.S. at 844. In this case, Congress explicitly delegated to the FCC the task of setting the national limit, and the court should have deferred to the FCC's reasonable construction of section 533(f).

1. The FCC interpreted section 533(f) as directing it to consider diversity when setting the ownership limits. App. 267-269, 280. It explicitly rejected the view that Congress intended the FCC to focus on antitrust principles to the exclusion of its traditional public interest review, concluding that to do so would nullify four of the seven factors Congress included in §533(f)(2). App. 280; *Time Warner I*, 211 F.3d at 1316.

Although the court expressly acknowledged that the lan-

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[18] "It is well understood that when there are two reasonable constructions for a statute, yet one raises a constitutional question, the Court should prefer the interpretation which avoids the constitutional issue." *Legal Services Corp. v. Velazquez*, 121 S.Ct. 1043, 1050 (2001) (*citing Gomez v. United States*, 490 U.S. 858, 864 (1989)); *See also Frisby v. Schultz*, 487 U.S. 474, 483 (noting that departure from this principle is "plain error") (1988).

guage it found controlling was "extremely vague," App. 15, it ignored the FCC's analysis.

The FCC's decision was far more reasonable than the court's. The Commission read the law as directing use of a traditional public interest analysis to remediate levels of concentration which might be considered "safe" under traditional antitrust analysis. App . 267-69 (relying on H.Rep at 42). This accords with the interpretation given to §11(c), and the 1992 Act generally, by the courts. *Turner II*, 520 U.S. at 198-90; *Time Warner I*, 211 F.3d at 1319-20. By contrast, Congress never used the word "collusion."

2. The legislative history shows that the drafters of the legislation did not intend to sever §11(c) from the FCC's general public interest authority. The Senate Report observed that "[a]lthough the FCC has the authority to impose horizontal limitations on the cable industry (both national and regional), it has not done so." S.Rep. at 34. As a result, "to address the issue of national concentration in the cable industry and enhance effective competition, the legislation directs the FCC to place reasonable limits on the size of MSOs." *Id.* The drafters intended that the legislation give "the FCC flexibility to determine what limits are reasonable ***and in the public interest***." *Id.* (emphasis added). This understanding is echoed in the section-by-section analysis. *Id.* at 80.

When considering the need for a horizontal limit, the Senate Report identified two concerns: that "concentration of the media in the hands of a few" would allow "media gatekeepers" to control information and foreclose avenues for "unorthodox or unpopular speech"; and that horizontal concentration "can be the basis of anticompetitive acts." S.Rep. at 32-33. It further noted that "Federal policy has always been vigilant to restrain concentration when it threatened diversity of voices even though it did not rise to the level of an anti-trust violation." *Id.*

at 32-33.

In considering an analogous provision, the House Report also rejected "traditional antitrust analysis," stating that "diversity of information sources can only be assured by imposing limits ... substantially below those that traditional antitrust analysis would support." H.R. Rep. at 42. The analysis concludes that "competition is essential ***both*** for ensuring diversity ... ***and*** for protecting consumers." Accordingly, "steps must be taken to encourage robust competition in the video programming marketplace." *Id.* at 44.

Thus, Congress clearly intended to promote diversity through the horizontal ownership limit. The drafters viewed the purpose of "enhancing effective competition" as the mechanism by which diversity is preserved and enhanced. *See also Time Warner I*, 211 F.3d at 1319-20. The court below, by substituting its judgment for that of the agency's, nullified this Congressional intent. By doing so, the panel undermined fundamental statutory policy designed to prevent "anticompetitive acts" and the creation of powerful "media gatekeepers." S.Rep. at 32-33.

III. THE PANEL FAILED TO AFFORD SUBSTANTIAL DEFERENCE TO THE PREDICTIVE JUDGMENT OF CONGRESS AND THE FCC.

The panel's failure to afford substantial deference to the predictive judgment of Congress and the FCC squarely conflicts with this Court's decisions in *NCCB*, *Turner I* and *II*, and other precedents. In so doing, the panel improperly dismissed the FCC's reliance on its decades of experience regulating the cable industry, as well as commonly accepted economic principles concerning concentrated markets and anti-competitive behavior. The result is an intermediate in theory, but strict in fact, *O'Brien* standard of review that more closely resembles the strict scrutiny reserved for content-based regulations. The

panel's new standard strips Congress and the FCC of the flexibility necessary to adequately respond to the complicated issues presented by telecommunications regulation, preventing it from properly balancing the free speech interests at stake.

A. The Panel's Rejection of the Predictive Judgments of Congress and the FCC Sharply Departs From This Court's First Amendment Jurisprudence.

When reviewing the constitutionality of a statute, "courts must accord substantial deference to the predictive judgments of Congress." *Turner I*, 520 U.S. at 195 (citations omitted). Similarly, when "evaluating the First Amendment claims of respondents [this Court] must afford great weight to the decisions of Congress and the experience of the Commission." *Columbia Broad. Sys. v. Democratic Nat. Comm.*, 412 U.S. 94, 102 (1973); *Turner II*, 520 U.S. at 196.533(f).

1. In 1992, Congress determined that without preemptive action, the cable industry would reach a level of concentration inimical to the public interest. 1992 Cable Act, §2(a)(4); S.Rep. at 32-34. Congress made the underlying predictive judgment that a prophylactic cap on the number of subscribers a single cable operator could reach was necessary to preserve a diversity of outlets in the market, as well as safeguard against anticompetitive effects associated with highly concentrated markets with barriers to entry such as cable. 1992 Cable Act, §11(c); *Time Warner I*, 211 F.3d at 1320. Accordingly, Congress directed the FCC to set a reasonable limit to further these important interests.

The panel effectively contravenes Congress' fundamental predictive judgment concerning concentration and the cable industry. As demonstrated above, it frustrated Congressional directives by sharply limiting the FCC's authority under the statute to set a limit based on diversity concerns. As explained below, the panel failed to defer to the FCC's expertise, an

expertise Congress intended the FCC to exercise in setting a pro-diversity, pro-competitive floor in the cable market. This is flatly inconsistent with this Court's precedents. *Turner II*, 520 U.S. at 224 ("Judgments about how competing economic interests are to be reconciled in the complex and fast-changing field of television are for Congress to make.")

2. When factual determinations of the FCC are "primarily of a judgmental or predictive nature ... complete factual support in the record for the Commission's judgment or prediction is not possible or required; a forecast of the direction in which future public interest lies necessarily involves deductions based on the expert knowledge of the agency." *NCCB*, 436 U.S. at 813-14 (citations and internal quotes omitted); *FCC v. WNCN Listeners Guild*, 450 U.S. 582, 594-96 (1981); *Turner I*, 512 U.S. at 665 (citing *NCCB*, 436 U.S. at 814); *cf. Baltimore Gas & Electric Co. v. Nat'l Res. Def. Council*, 462 U.S. 87, 103(1983)("court must generally be at its most deferential" when reviewing predictions within agency's expertise).

The panel held that the FCC had not provided sufficient evidence demonstrating a risk of collusion. App. at 10. This is in clear conflict with NCCB; in upholding the FCC's newspaper-broadcast cross-ownership rule under a First Amendment challenge, this Court held that the "the [FCC] was *entitled to rely on its judgment, based on experience*, that it is unrealistic to expect true diversity from a commonly owned station-newspaper combination." *NCCB*, 436 U.S. at 796-97 (citations and internal quotations omitted) (emphasis added). This Court rejected claims that the FCC needed to "conclusively establish" that the rule would lead to viewpoint diversity. *Id.* Rather, it emphasized deference to the FCC's predictive judgment because "[d]iversity and its effects are ... elusive concepts ... evidence of specific abuses by common owners is difficult to compile [and] the possible benefits of competition do not lend themselves to

detailed forecast." *Id.*

Given the Congressional directive to adopt an ownership cap, the FCC is entitled to even greater deference here than in *NCCB*, where the agency was invoking generic statutory powers. The FCC used its extensive expertise with the cable industry to predict that a high level of concentration would raise too great a threat to diversity and too high a risk of anti-competitive behavior. *NCCB*, 436 U.S. at 796-97; *Marsh Media v. FCC*, 798 F.2d 772, 776 (5th Cir. 1986) *cert. denied*, 479 U.S. 1085 (1987) (rejecting First Amendment challenge to broadcast TV-cable cross ownership rule based on predictive judgment); *see City of Erie, et al. v. Pap's A.M., TDBA "Kandyland,"* 529 U.S. 277, 297 (2000)(referring to FCC's "special firsthand knowledge" of cable industry and citing *NCCB*, 436 U.S. at 775). Implementing legislation designed to *prevent* anti-competitive practices is precisely the situation that calls for substantial deference. *Turner II*, 520 U.S. at 225 (Stevens, J. concurring) (emphasizing deference to judgments concerning "forestalling the abuse of monopoly power..."). As in *NCCB*, demanding evidence of collusion *a priori* is "difficult to compile" and would defeat the prophylactic purpose of § 11(c).

In the decision under review, the FCC applied its familiarity with video markets to the rulemaking record. App. 281-88. This produced several possible percentages, *id.* 285-290, which it narrowed to three-20%, 30%, or 40%-after weighing Congress' concerns with preserving efficiencies of scale for cable operators and the threats concentration posed to competition and diversity. *Id.* The FCC ultimately concluded that a 30% limit would best ensure the availability of new programming services and preserve a reasonable level of diversity. *See* discussion *supra* at 9-10; App. 289-91. The 30% limit also addressed the unilateral effects a large operator may have on the market. *Id.* at 138, 295.

The court improperly second-guessed the FCC's predictive judgment in balancing the competing interests involved to set a pro-competitive, pro-diversity floor for the cable industry. *WNCN*, 450 U.S. at 594-96 (affirming the FCC's predictive judgment "assess[ing] the benefits and harms likely to flow from Government review of entertainment programming ..."); *United States v. Midwest Video Corp.*, 406 U.S. 649, 674 (1972); *cf.*, *Turner II*, 520 U.S. at 224.

3. The reasonableness of the FCC's predictive judgment is further supported by its reliance on economic principles concerning the anti-competitive risks of concentrated markets. When reviewing First Amendment challenges, this Court has noted that "[t]he quantum of empirical evidence needed to satisfy heightened scrutiny of legislative judgment will vary up or down with the novelty and plausibility of the justification raised." *Nixon v. Shrink Missouri Gov. PAC*, 528 U.S. 377, 391 (2000). The FCC relied on accepted economic principles to conclude that a 30% limit would substantially reduce the likelihood of explicit or implicit coordinated activity between large cable operators because such "activity ... is more likely with few firms than many (due to greater ease in reaching consensus, monitoring compliance, and punishing cheaters), and such behavior will have a greater impact the larger combined share of the market these firms control." App. 295-96, 139. Such a proposition is "neither novel nor implausible." *Nixon*, 528 U.S. at 391 (characterizing the legislature's judgment regarding the effect of money on the political process). This Court has deferred in other First Amendment contexts to the predictive judgments of lawmakers centering on commonly accepted principles. *Id.* at 391-396; *Burson v. Freeman*, 504 U.S. 191, 208-211 (1992). The FCC should not be held to a higher standard.

While the panel discounts predictive judgments based on the level of concentration in a market, App. at 11-12, structural

market analysis is a linchpin of antitrust law. "Merger law, 'rests upon the theory that, where rivals are few, firms will be able to coordinate their behavior, either by overt collusion or implicit understanding, in order to restrict out put and achieve profits above competitive levels." *FTC v. H. J. Heinz Co.*, 246 F.3d 708, 719 (D.C. Cir. 2001)(citations omitted).[19] For instance, the DOJ/FTC Merger Guidelines rely on market concentration to determine the potential anti-competitive dangers of a proposed merger. U.S. Dep't of Justice & Federal Trade Comm'n, *Horizontal Merger Guidelines*,§ 1.5 (1992), as revised (1995).

The FCC employed these principles to set a limit to prevent the cable market from consolidating to a level that would present the anti-competitive harms associated with highly concentrated markets with large barriers to entry, such as cable. App. 291-293. "The combination of a concentrated market and barriers to entry is a recipe for price coordination." *H. J. Heinz Co.*, 246 F.3d at 724 (citations omitted). The FCC's concern with setting a limit preempting tacit coordination is especially supported by accepted economic principles. *Id.* (quoting 4 Areeda, *et al.*, ANTITRUST LAW ¶901b2, at 9 (rev. ed. 1998) ("central object of merger policy [is] to obstruct the creation or reinforcement by merger of ... oligopolistic market structures in which tacit coordination can occur."). The FCC's selection of 30% is consonant with the Merger Guidelines as well. Under the Guidelines, even a market less concentrated than one

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[19] *See also United States v. General Dynamics*, 415 U.S. 486, 497 (1974) (emphasizing *prima facie* anti-competitive threats of highly concentrated markets); Sullivan & Grimes, THE LAW OF ANTITRUST: AN INTEGRATED HANDBOOK 530 (2000) ("The rule of thumb...is that the more concentrated an industry, the more likely is oligopolistic behavior...For example, a ten-firm industry is more likely to require some sort of coordination...whereas the three-firm industry might more easily maintain prices through parallel behavior without express coordination.").

allowed by the FCC's cap would be highly concentrated and presumptively indicate a high risk of anti-competitive effects.[20]

Contrary to the panel's implication, the FCC did not act in a vacuum when it selected the 30% limit to create a prophylaxis to ensure diversity and enhance competition. App. 11 (rejecting conclusion "that ... collusion is less likely when there are more firms ...[because] ...by itself it lends no insight into the question of what the appropriate horizontal limit is."). As discussed above, the FCC applied these principles within the narrow context of deciding between a cap ensuring at least five (20%), four (30%), or three (40%) material operators in the market. Further, the record evinces barriers to entry for new programmers, App. 291-93, a trend toward concentration in the market, *see* discussion *supra* at 9, and a web of inter-connected relationships between operators, *id.* at 5-6. These factors make it particularly appropriate for the FCC to have employed economic principles to bolster its analysis.

Finally, other panels of the D.C. Circuit have deferred to predictive judgments forecasting anti-competitive practices in the cable industry founded on basic economic principles. In *Time Warner I*, the D.C. Circuit deferred to the predictive judgment of Congress that the concentrated cable market posed a risk to diversity and competition to uphold the constitutionality of §11(c). 211 F. 3d at 1319-1320.

B. The Court's Repudiation of the FCC's Predictive Judgment Creates a Standard Which is Intermediate in Theory,

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[20]Under the Guidelines, market concentration is measured by HHI. The Guidelines cite a market with four firms with market shares of 30%, 30%, 20% and 20% as highly concentrated with an HHI of 2600. *Merger Guidelines* § 1.5 n.17. A 30% limit is also consistent with the other standard measurement of market concentration-the Four Firm Concentration Ratio. *See* Shepard, THE ECONOMICS OF INDUSTRIAL ORGANIZATION 4 (1985) (market where leading four firms have in excess of 60% is considered highly concentrated).

but Strict in Fact.

The cable ownership limits are content-neutral. *Time Warner I*, 211 F.3d at 1317-18; App. 6. And as this Court has held, content-neutral rules "do not pose such inherent dangers to free expression, or present such potential for censorship ... as to justify application of the most exacting level of First Amendment scrutiny." *Turner I*, 512 U.S. at 661. Structural regulations like the ownership limits foster Congress' diversity goals in a content-neutral manner without raising the specter of government censorship. S.Rep. at 50; *Review of the Commission's Regulations Governing Television Broadcasting*, 14 FCC Rcd 12903, 12915 (1999). For this reason, structural media regulations are reviewed under the more lenient *O'Brien* standard. *Id.*, at 12915 (citing *NCCB*, 436 U.S at 801; *Turner II*, 520 U.S. at 189)).

1. In dismissing the FCC's reliance on its expertise and accepted economic principles to set the 30% ownership limit, the panel effectively elevated the *O'Brien* intermediate standard of review to a level more closely resembling the strict scrutiny reserved for content-based rules. This new standard is driven by an overly demanding substantial evidence requirement of the "harm" prong of *O'Brien* intermediate scrutiny. It strips the FCC of the necessary flexibility to implement Congressionally mandated, prophylactic, content-neutral structural regulations. Precluding the FCC from employing accepted economic principles to *predict* anti-competitive behavior substantially hobbles the FCC's ability to promulgate rules *preventing* such harms.

A plurality of this Court has cautioned against the application of First Amendment norms in the media context that would "impose judicial formulas *so rigid that they become a straightjacket that disables government from responding to serious problems.*" *Denver Area Educ. Telecomm. Consortium, Inc. v. FCC*, 518 U.S. 727, 741 (1996) (Breyer, J., joined by Stevens, O'Connor and Souter, J.J. concurring in judgment and concurring in part)

(emphasis added). The court's misconstruction of *O'Brien* intermediate scrutiny does precisely what *Denver Area* instructs not to do. By sharply limiting the FCC's ability to act preemptively, the panel's new standard "lack[s] the flexibility necessary to allow government to respond to very serious practical problems ...." *Denver Area*, 518 U.S. at 740; *cf. Bartnicki v. Hopper*, 121 S Ct. 1753, 1768 (2001)("In my view, the Constitution permits legislatures to respond flexibly to the challenges future technology may pose to the individual's interest in basic personal privacy.") (Breyer, J., joined by O'Connor, J., concurring).

2.. Moreover, hamstringing the flexibility of the FCC prevents it from properly balancing the competing free speech interests implicated in this case. "In such circumstances, *where a law significantly implicates competing constitutionally protected interests in complex ways the Court ... has balanced interests.*" *Nixon*, 528 U.S. at 402 (Breyer, joined by Ginsburg, J.J., concurring) (emphasis added). In fact, this Court has consistently balanced the relevant free speech interests when reviewing First Amendment challenges to media regulations. *See, e.g., Turner II*, 520 U.S. at 192-194 (recognizing the speech interests of both viewers and cable operators) and at 224-229 (Breyer, J., concurring in part) (balancing "the important First Amendment interests on both sides of the equation "); *Columbia Broad. Syst.*, 412 U.S. at 102-103 ("Balancing the various First Amendment interests involved in the broadcast media ....").

The court radically departed from this body of caselaw by solely considering the free speech interests of cable operators. The panel's First Amendment analysis focused exclusively on the modest infringement the 30% limit imposed on cable operators' freedom of expression.[21] In contrast, the panel ignored the

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[21]The 30% limit excludes new subscribers gained from "overbuilding," the construction of a second cable system in an area already served by an

free speech interests of the key beneficiaries of the 1992 Act–the viewing public and independent programmers.

In sum, the court' decision demonstrably tilts the scale in favor of the cable operator, and indeed any entity challenging the FCC's structural media regulations. In so doing, it blurs the distinction between the strict scrutiny applied to content-based restrictions of speech and the traditionally more relaxed level of review applied to content-neutral regulations.[22] In this way, the panel's holding is reminiscent of the long since repudiated doctrine of *Lochner v. New York*, 198 U.S. 45 (1905) employed by this Court to strike down socio-economic legislation "based on the Court's own notions of the most appropriate means for the State to implement its considered policies." *Central Hudson*, 447 U.S. at 589 (Rehnquist, C.J. dissenting). Accordingly, this Court should review the panel's decision.

CONCLUSION

The petition for writ of certiorari should be granted.

Respectfully submitted,

Andrew Jay Schwartzman
(Counsel of Record)
Cheryl A. Leanza
Harold J. Feld

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incumbent operator. App. 279. Thus, the limit *does not* prevent an operator from speaking directly to 100% of the country, as long as it competes with, rather than buys, the incumbent monopoly provider for any subscribers over the limit.

[22] *Cf. Central Hudson Gas & Elec. Corp. v. Public Service Comm. of New York*, 447 U.S. 557, 589 (1980)(Rehnquist, C.J., dissenting)(citing similar concerns with "fail[ing] to give due deference to th[e] subordinate position of commercial speech" as representing a "return[] to the bygone era of *Lochner*").

Media Access Project
950 18th St., Suite 220
Washington, D.C. 20006
(202) 232-4300

Fernando Bohorquez, Jr.
Angela J. Campbell
Institute for Public Representation
Georgetown University Law Center
600 New Jersey Ave., NW
Suite 312
Washington, DC 20001
(202) 662-9535
Counsel for Consumer Federation of America, et al.

August 2, 2001

Supreme Ct.

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NO. _____

IN THE

Supreme Court of the United States

TIME WARNER ENTERTAINMENT COMPANY, L.P., *et al.*,
Petitioners,

v.

FEDERAL COMMUNICATIONS COMMISSION AND
UNITED STATES OF AMERICA,
Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

PETITIONERS' APPENDIX
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FERNANDO BOHORQUEZ, JR.
ANGELA J. CAMPBELL
INSTITUTE FOR PUBLIC REPRESENTATION,
GEORGETOWN UNIVERSITY LAW CENTER
600 New Jersey Ave., NW
Suite 312
(202) 662-9535

ANDREW JAY SCHWARTZMAN
(Counsel of Record)
CHERYL A. LEANZA
HAROLD J. FELD
MEDIA ACCESS PROJECT
950 18TH ST., SUITE 220
Washington, D.C. 20006
(202) 232-4300

Counsel for Consumer Federation of America, et al.

August 2, 2001

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App. 1

United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

Argued October 17, 2000 Decided March 2, 2001

No. 94-1035

TIME WARNER ENTERTAINMENT CO., L.P.

PETITIONER

v.

FEDERAL COMMUNICATIONS COMMISSION AND

UNITED STATES OF AMERICA,

RESPONDENTS

BELLSOUTH CORPORATION, ET AL.,

INTERVENORS

Consolidated with

95-1337, 99-1503, 99-1504, 99-1522,

99-1541, 99-1542, 00-1086

On Petitions for Review of Orders of the

Federal Communications Commission

David W. Carpenter argued the cause for petitioners AT&T Corporation and Time Warner Entertainment Co., L.P. With him on the briefs were *Peter Keisler, David L. Lawson, C. Frederick Beckner III, Henk Brands* and *Robert D. Joffe. Charles S. Walsh, Richard B Beckner, Stuart W. Gold* and *Marc C. Rosenblum* entered appearances.

Robert D. Joffe and *Henk Brands* were on the briefs for petitioner Time Warner Entertainment Co., L.P. *Charles S. Walsh, Richard B. Beckner* and *Stuart W. Gold* entered appearances.

Andrew Jay Schwartzman, Cheryl A. Leanza and *Harold Feld* were on the briefs for petitioner Consumers Union.

James M. Carr, Counsel, Federal Communications Com- mission, argued the cause for respondents. With him on the brief were *Christopher J. Wright*, General Counsel, *Daniel M. Armstrong*, Associate General Counsel, *Joel Marcus* and *James M. Carr*, Counsel, *David W. Ogden*, Acting Assistant Attorney General, U.S. Department of Justice, *Mark*

B. Stern and *Jacob M. Lewis*, Attorneys, and *Wilma A. Lewis*, U.S. Attorney. *William E. Kennard*, General Counsel, Federal Communications Commission, *John E. Ingle*, Deputy Associate General Counsel, and *Catherine G. O'Sullivan*, *Robert B. Nicholson* and *Robert J. Wiggers*, Attorneys, U.S. Department of Justice, entered appearances.

Henk J. Brands, *Robert D. Joffe*, *Peter D. Keisler*, *David L. Lawson* and *C. Frederick Beckner III* were on the brief for intervenor Time Warner Entertainment Co., L.P. in No. 99-1522. *Mark C. Rosenblum* entered an appearance.

Before: WILLIAMS, RANDOLPH and TATEL, *Circuit Judges*.

Opinion for the Court filed by *Circuit Judge* WILLIAMS.

WILLIAMS, *Circuit Judge*: Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460 ("1992 Cable Act"), amends 47 U.S.C. § 533 to direct the Federal Communications Commission to set two types of limits on cable operators. The first type is horizontal, addressing operators' scale: "limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such person, or in which such person has an attributable interest." 47 U.S.C. § 533(f)(a)(1)(A). The second type is vertical, addressing operators' integration with "programmers" (suppliers of programs to be carried over cable systems): "limits on the number of channels on a cable system that can be occupied by a video programmer in which a cable operator has an attributable interest." 47 U.S.C. § 533(f)(a)(1)(B). The FCC has duly promulgated regulations. See 47 C.F.R. § 76.503-04. Petitioners Time Warner and AT&T challenge the horizontal limit as in excess of statutory authority, as unconstitutional infringements of their freedom of speech, and as products of arbitrary and capricious decisionmaking which violate the Administrative Procedure Act. Time Warner similarly challenges the vertical limit. Together with AT&T, Time Warner also challenges as arbitrary and capricious the rules for determining what counts as an "attributable interest." Concluding that the FCC has not met its burden under the First Amendment and, in part, lacks statutory authority for its actions, we remand for further consideration of both limits. In addition we vacate specific portions of the attribution

rules as lacking rational justification.

Consumers Union also files a petition for review, which need not detain us long. It objects to the Commission's action to the extent that it continued a stay on enforcement of the horizontal limit. See *Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992*, 14 F.C.C.R. 19098, 19127-28 ¶ ¶ 71-73 (1999) ("Third Report"). The Commission issued the stay after a district court found the statute underlying that limit unconstitutional, see *Daniels Cablevision, Inc. v. United States*, 835 F. Supp. 1 (D.D.C. 1993), and provided that in the event of *Daniels*'s reversal the stay would end. See *Implementation of Sections 11 and 13 of the Cable Television Consumer Protection and Competition Act of 1992*, 8 F.C.C.R. 8565, 8609 ¶ 109 (1993) ("Second Report"). We did reverse *Daniels* in *Time Warner Entertainment Co. v. United States*, 211 F.3d 1313 (D.C. Cir. 2000) ("*Time Warner I*"), so the stay ended automatically.[1] Thus the stay issue is moot unless the issue posed is capable of repetition yet evading review. Even if we assume that the issue evades review, its recurrence is not probable enough to qualify it as "capable of repetition." See *Spencer v. Kemna*, 523 U.S. 1, 17 (1998) (requiring "a reasonable expectation that the same complaining party [will] be subject to the same action again") (internal citations omitted). Although we find here that the regulations fail constitutional scrutiny, the specific condition that led to the stay – a pending challenge to the *statute*'s constitutionality – is highly unlikely to recur. We therefore find Consumers Union's claim moot and dismiss the petition.

* * *

The horizontal rule imposes a 30% limit on the number of

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[1]The cross-appeals of the government and the cable firms from the district court's decision in *Daniels* were originally consolidated with the cable firms' petitions for review of earlier iterations of the implementing regulations. See *Time Warner I*, 211 F.3d at 1315-16. After a date for oral argument was set, the FCC initiated a new rulemaking as part of its planned quinquennial review of the horizontal regulations. We therefore severed the *Daniels* appeals from the challenges to the regulations, holding the latter in abeyance until the completion of the new rulemaking. See *id.* The challenge to the new horizontal rules has supplanted that portion of the earlier challenges.

subscribers that may be served by a multiple cable system operator ("MSO"). See 47 C.F.R. § 76.503; *Third Report* 14 F.C.C.R. at 19119 ¶ 55. Both the numerator and denominator of this fraction include only current subscribers to multichannel video program distributor ("MVPD") services. See *id.* at 19107-10 ¶ ¶ 20-25. Subscribers include not only users of traditional cable services but also subscribers to non-cable MVPD services such as Direct Broadcast Satellite ("DBS"),[2] a rapidly growing segment of the MVPD market. See *id.* at 19110-12 ¶ ¶ 26-35. The Commission pointed out that under this provision the nominal 30% limit would allow a cable operator to serve 36.7% of the nation's cable subscribers if it served none by DBS. See *id.* at 19113 ¶ 37 & n.82.[3] In an express effort to encourage competition through new provision of cable, the Commission excluded from any MSO's numerator all new subscribers signed up by virtue of "overbuilding," the industry's term for cable laid in competition with a pre-existing cable operator. See *id.* at 19112-13 ¶ ¶ 34, 37. Further, subscribers to a service franchised after the rule's adoption (October 20, 1999) do not go into an MSO's numerator, even if not the result of an overbuild. See *id.* at 19112 ¶ 33. As a result, the rule's main bite is on firms obtaining subscribers through merger or acquisition.

The vertical limit is currently set at 40% of channel capacity, reserving 60% for programming by non-affiliated firms. See 47 C.F.R. § 76.504; *Second Report*, 8 F.C.C.R. at 8593- 94 ¶ 68; *Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition*

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[2]DBS "is a nationally distributed subscription video service that delivers programming via satellite to a small parabolic 'dish' antenna located at the viewer's home." *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Program ming*, Seventh Annual Report, CS Docket No. 00-132, FCC 01-01 (rel. Jan. 8, 2001) ¶ 71 (2000) ("Seventh Annual Report").

[3]30% of roughly 80 million MVPD subscribers would be about 24 million subscribers, which in turn would be 36.69% of roughly 66 million cable subscribers. Under the Commissions most recent subscriber estimates, this provision would allow an MSO to serve 37.4% of cable subscribers, or approximately 1.1 million more customers than when the *Third Report* was written. See *Seventh Annual Report* at ¶ ¶ 6-7.

Act of 1992, 10 F.C.C.R. 7364, 7368 ¶ 14 (1995) ("Reconsideration Order"). Channels assigned to broadcast stations, leased access, and for public, educational, or governmental uses are included in the calculation of channel capacity. See *id.* at 7371-73 ¶¶ 20- 27. Capacity over 75 channels is not subject to the limit, so a cable operator is never required to reserve more than 45 channels for others (.60 x 75 = 45). See *id.* at 7374-76 ¶¶ 31-35.

As cable operators, Time Warner and AT&T "exercise[ ] editorial discretion in selecting the programming [they] will make available to [their] subscribers," *Time Warner I*, 211 F.3d at 1316, and are "entitled to the protection of the speech and press provisions of the First Amendment," *Turner Broadcasting System, Inc. v. Federal Communications Commission*, 512 U.S. 622, 636 (1994) ("*Turner I*") (quoting *Leathers v. Medlock*, 499 U.S. 439, 444 (1991)). The horizontal limit interferes with petitioners' speech rights by restricting the number of viewers to whom they can speak. The vertical limit restricts their ability to exercise their editorial control over a portion of the content they transmit.

In *Time Warner I* we upheld the statutory provisions against a facial attack, after finding them subject to intermediate rather than, as the cable firms argued, strict scrutiny. *Time Warner I*, 211 F.3d at 1316-22. The regulations here present a related but independent set of questions. Constitutional authority to impose some limit is not authority to impose any limit imaginable.

In briefs written before the issuance of *Time Warner I*, petitioners argued here for strict scrutiny. At oral argument they withdrew from this position and said, euphemistically, that they were "happy to stand on intermediate scrutiny." Because of that concession and, in any event, not seeing any distinction between the statute and the regulations for level of-scrutiny purposes, we apply intermediate scrutiny. Under the formula set forth in *United States v. O'Brien*, 391 U.S. 367, 377 (1968), and reaffirmed by *Turner Broadcasting System, Inc. v. Federal Communications Commission*, 520 U.S. 180, 189 (1997) ("*Turner II*"), a governmental regulation subject to intermediate scrutiny will be upheld if it "advances important governmental interests unrelated to the suppression of free speech and does not burden substantially more

speech than necessary to further those interests." *Id.* (quoting *O'Brien*, 391 U.S. at 377).

The interests asserted in support of the horizontal and vertical limits are the same interrelated interests that we found sufficient to support the statutory scheme in *Time Warner I*: "the promotion of diversity in ideas and speech" and "the preservation of competition." *Time Warner I*, 211 F.2d at 1319; see also *Turner I*, 512 U.S. at 662-64 (concluding that both qualify as important governmental interests). After a review of the legislative history, we concluded that Congress had drawn "reasonable inferences, based upon substantial evidence, that increases in the concentration of cable operators threatened diversity and competition in the cable industry." *Time Warner I*, 211 F.3d at 1319-20. But the FCC must still justify the limits that it has chosen as not burdening substantially more speech than necessary. In addition, in "demonstrat[ing] that the recited harms are real, not merely conjectural," *Turner I*, 512 U.S. at 664, the FCC must show a record that validates the *regulations*, not just the abstract statutory authority.

* * *

The FCC asserts that a 30% horizontal limit satisfies its statutory obligation to ensure that no single "cable operator or group of cable operators can unfairly impede ... the flow of video programming from the video programmer to the consumer," 47 U.S.C. § 533(f)(2)(A), while adequately respecting the benefits of clustering[4] and the economies of scale that are thought to come with larger size. See *Third Report*, 14 F.C.C.R. at 19123-24 ¶ 61. It interpreted this statutory language as a directive to prohibit large MSO—either by the action of a single MSO or the coincidental or collusive actions of several MSO—from precluding the entry into the market of a new cable programmer. See *id.* at

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[4]"Clustering" refers to the strategy under which MSO concentrate their operations within a particular geographic region, giving up scattered holdings around the country. The benefits are thought to be in achieving economies of both scale and scope, allowing MSO to spread fixed investment costs over a larger customer base and to better compete with telephone companies owning local loops that are actual or potential substitutes. See *Seventh Report* ¶ ¶ 152-53.

19116 ¶ 43. In setting the limit at 30%, it assumed there was a serious risk of collusion. See *id.*, Part VI, at 19113-25 ¶¶ 36-65. But while collusion is a form of anti-competitive behavior that implicates an important government interest, the FCC has not presented the "substantial evidence" required by *Turner I* and *Turner II* that such collusion has in fact occurred or is likely to occur; so its assumptions are mere conjecture. See *Turner II*, 520 U.S. at 195 (citing *Turner I*, 512 U.S. at 666). The FCC alternatively relies on its supposed grant of authority to regulate the non-collusive actions of large MSOs. Congress may indeed, under certain readings of *Turner I* and *Turner II*, have the power to regulate the coincidental but independent actions of cable operators solely in the interest of diversity, but "[where an administrative interpretation of a statute invokes the outer limits of Congress' power, we expect a clear indication that Congress intended that result." *Solid Waste Agency v. United States Army Corps of Angriest*, __ U.S. __, 121 S. Ct. 675, 683 (2001). The 1992 Cable Act, as we shall see, instead expresses the contrary intention.

Part VI of the *Third Report* lays out the calculations that lead the FCC to the 30% limit. See *Third Report*, Part VI, 14 F.C.C.R. at 19113-25 ¶¶ 36-65. First the FCC determines that the average cable network needs to reach 15 million subscribers to be economically viable. See *id.* at 19114-16 ¶¶ 40-42. This is 18.56% of the roughly 80 million MVPD subscribers, and the FCC rounds it up to 20% of such subscribers. The FCC then divines that the average cable programmer will succeed in reaching only about 50% of the subscribers linked to cable companies that *agree* to carry its programming, because of channel capacity, "programming tastes of particular cable operators," or other factors. *Id.* at 19117-18 ¶ 49. The average programmer therefore requires an "open field" of 40% of the market to be viable (.20/.50 = .40). See *id.* at 19117-18 ¶¶ 46-50.

Finally, to support the 30% limit that it says is necessary to assure this minimum, the Commission reasons as follows: With a 30% limit, a programmer has an "open field" of 40% of the market even if the two largest cable companies deny carriage, acting "individually or collusively." *Id.* at 19119 ¶ 53. A 50% rule is inadequate because, if a

duopoly were to result, "[t]he probability of tacit collusion is higher with 2 competitors than 3 competitors." *Id.* at 19118-19 ¶ 51. Even if collusion were not to occur, *independent* rejections by two MSOs could doom a new programmer, thwarting congressional intent as the Commission saw it. See *id.* A 40% limit is insufficient for the same reason: "two MSOs, ... representing a total of 80% of the market, might decline to carry the new network" and leave only 20% "open," which by hypothesis is not enough (because of the 50% success rate). *Id.* at 19119 ¶ 52. Although the Commission doesn't spell out the intellectual process, it is necessarily defining the requisite "open field" as the residue of the market after a programmer is turned down either (1) by one cable company acting alone, or (2) by a set of companies acting either (a) collusively or (b) independently but nonetheless in some way that, because of the combined effect of their choices, threatens fulfillment of the statutory purposes. We address the FCC's authority to regulate each of these scenarios in turn.

The Commission is on solid ground in asserting authority to be sure that no single company could be in a position singlehandedly to deal a programmer a death blow. Statutory authority flows plainly from the instruction that the Commission's regulations "ensure that no cable operator or group of cable operators can unfairly impede, either because of *the size of any individual operator* or because of joint actions of operators of sufficient size, the flow of video programming from the video programmer to the consumer." 47 U.S.C. § 533(f)(2)(A) (emphasis added). Constitutional authority is equally plain. As the Supreme Court said in *Turner II*: "We have identified a corresponding 'governmental purpose of the highest order' in ensuring public access to 'a multiplicity of information sources.' " 520 U.S. at 190 (quoting *Turner I*, 512 U.S. at 663); see also *Time Warner Entertainment Co. v. Federal Communications Commission*, 93 F.3d 957, 969 (D.C. Cir. 1996). If this interest in diversity is to mean anything in this context, the government must be able to ensure that a programmer have at least two conduits through which it can reach the number of viewers needed for viability—independent of concerns over anticompetitive conduct.

Assuming the validity of the premises supporting the FCC's

conclusion that a 40% "open field" is necessary (a question that we need not answer here), the statute's express concern for the act of "any individual operator" would justify a horizontal limit of 60%. To reach the 30% limit, the FCC's action necessarily involves one or the other of two additional propositions: Either there is a material risk of collusive denial of carriage by two or more companies, or the statute authorizes the Commission to protect programmers against the risk of completely *independent* rejections by two or more companies leaving less than 40% of the MVPD audience potentially accessible. Neither proposition is sound.

First, we consider whether there is record support for inferring a non-conjectural risk of collusive rejection. Either Congress or the Commission could supply that record, and we take them in that order. We give deference to the predictive judgments of Congress, see *Turner II*, 520 U.S. at 195-96 (citing *Turner I*, 512 U.S. at 665), but Congress appears to have made no judgment regarding collusion. The statute plainly alludes to the *possibility* of collusion when it authorizes regulations to protect against "*joint* actions by a group of operators of sufficient size." 47 U.S.C. § 533(f)(2)(A) (emphasis added). But this phrase, while granting the Commission authority to take action in the event that it finds collusion extant or likely, is not itself a congressional finding of actual or probable collusion. Such findings have not been made. No reference to collusion appears in the Act's findings or policy, see 1992 Cable Act § 2, 106 Stat. at 1460-63, nor in the legislative history discussing the horizontal or vertical limits. See H.R. Rep. No. 102-628, at 40-43 (1992) ("House Report"); S. Rep. No. 102-92, at 24-29, 32-34, reprinted in 1991 U.S.C.C.A.N. 1133, at 1156-62, 1165-67 ("Senate Report"). It was thus appropriate for the FCC to describe Congress's reference to "joint" action as merely a "legislative *assumption*." *Third Report*, 14 F.C.C.R. at 19116 ¶ 43 (emphasis added).

The Commission's own findings amount to precious little. It says only:

> The legislative assumption [about joint action] is not unreasonable given an environment in which all the larger operators in the industry are vertically integrated so that all are both buyers

> and sellers of programming and have mutual incentives to reach carriage decisions beneficial to each other. Operators have incentives to agree to buy their programming from one another. Moreover, they have incentives to encourage one another to carry the same non-vertically integrated programming in order to share the costs of such programming.

Id. None of these assertions is supported in the record. The Commission never explains why the vertical integration of MSOs gives them "mutual incentive to reach carriage decisions beneficial to each other," what may be the firms' "incentives to buy ... from one another," or what the probabilities are that firms would engage in reciprocal buying (presumably to reduce each other's average programming costs). After all, the economy is filled with firms that, like MSOs, display partial upstream vertical integration. If that phenomenon implies the sort of collusion the Commission infers, one would expect the Commission to be able to point to examples. Yet it names none. Further, even if one accepts the proposition that an MSO could benefit from sharing the services of specific programmers, programming is not more attractive for this purpose merely because it originates with another MSO's affiliate rather than with an independent.

The only justification that the FCC offers in support of its collusion hypothesis is the economic commonplace that, all other things being equal, collusion is less likely when there are more firms. See *Third Report* 14 F.C.C.R. at 19118-19 ¶ 51. This observation will always be true, although marginally less so for each additional firm; but by itself it lends no insight into the question of what the appropriate horizontal limit is. *Turner I* demands that the FCC do more than "simply 'posit the existence of the disease sought to be cured.' " *Turner I*, 512 U.S. at 664 (quoting *Quincy Cable TV, Inc. v. Federal Communications Commission*, 768 F.2d 1434, 1455 (D.C. Cir. 1985). It requires that the FCC draw "reasonable inferences based on substantial evidence." *Turner I*, 512 U.S. at 666. Substantial evidence does not require a complete factual record—we must give appropriate deference to predictive judgments that necessarily involve the expertise and experience of the agency. See *Turner II* 520 U.S. at 196, citing *Federal Commu-*

nications Commission v. National Citizens Comm. For Broadcasting, 436 U.S. 775, 814 (1978). But the FCC has put forth no evidence at all that indicates the prospects for collusion.

That having been said, we do not foreclose the possibility that there are theories of anti-competitive behavior other than collusion that may be relevant to the horizontal limit and on which the FCC may be able to rely on remand. See 47 U.S.C. § 533(f)(1). Indeed, Congress considered, among other things, the ability of MSOs dominant in specific cable markets to extort equity from programmers or force exclusive contracts on them. See 1992 Cable Act § 2(a)(4)-(5), 106 Stat. at 1460-61; Senate Report at 3, 14, 23-29, 32-34, reprinted in 1991 U.S.C.C.A.N. at 1135, 1146-47, 1156-62, 1165-67; House Report at 40-43. A single MSO, acting alone rather than "jointly," might perhaps be able to do so while serving somewhat less than the 60% of the market (i.e., less than the fraction that would allow it unilaterally to lock out a new cable programmer) despite the existence of antitrust laws and specific behavioral prohibitions enacted as part of the 1992 Cable Act, see 47 U.S.C. § 536, and the risk might justify a prophylactic limit under the statute. See *Time Warner I*, 211 F.3d at 1322-23. So the absence of any showing of a serious risk of collusion does not *necessarily* preclude a finding of a sufficient governmental interest in preventing unfair competition. (We express no opinion on whether exploitation of a monopoly position in a specific cable market to extract rents that would otherwise flow to programmers alone gives rise to an "important governmental interest" justifying a burden on speech.) But the FCC made no attempt to justify its regulation on these grounds.

We pause here to address an aspect of petitioners' statutory challenge that is relevant to a showing of non-conjectural harm. Congress required that in setting the horizontal limit, the FCC "take particular account of the market structure ... including the nature and market power of the local franchise." 47 U.S.C. § 533(f)(2)(C). Petitioners assert that the Commission's failure to take adequate account of the competitive pressures brought by the availability and increasing success of DBS make the horizontal limit arbitrary and capricious. Although DBS accounts for only 15.4% of current MVPD households,

the annual increase in its total subscribership is almost three times that of cable (nearly three million additional subscribers over the period June 1999 to June 2000, as against one million for cable). See *Seventh Annual Report* ¶ ¶ 6-8. To the extent petitioners argue that the horizontal limit must fail because market share does not *equal* market power, they misconstrue the statutory command. The Commission is not required to design a limit that falls solely on firms possessing market power.[5] The provision is directed to the Commission's intellectual process, and requires it, in evaluating the harms posed by concentration and in setting the subscriber limit, to assess the determinants of market power in the cable industry and to draw a connection between market power and the limit set.

It follows naturally from our earlier discussion that we do not believe the Commission has satisfied this obligation. Having failed to identify a non-conjectural harm, the Commission could not possibly have addressed the connection between the harm and market power. But the assessment of a real risk of anti-competitive behavior—collusive or not—is itself dependent on an understanding of market power, and the Commission's statements in the *Third Report* seem to ignore the true relevance of competition. In changing the calculation of the horizontal limit to reflect subscribers instead of homes at which a service is available, for instance, the Commission wrote:

> [W]hether subscribership or homes passed data is used is largely a mechanical issue in terms of the market power issue.... As the market develops in terms of competition we believe ... that an operator's actual number of subscribers more uniformly and accurately reflects pow-er in the programming marketplace. *Third Report*, 14 F.C.C.R. at 19108 ¶ 22.

But normally a company's ability to exercise market power depends not only on its share of the market, but also on the elasticities

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[5]Contrast Congress's requirement that the FCC "*make* such rules and regulations reflect the dynamic nature of the communications marketplace." 47 U.S.C. § 533(f)(2)(E) (emphasis added).

of supply and demand, which in turn are determined by the *availability* of competition. See *AT&T Corp. v. Federal Communications Commission*, 236 F.3d 729, 736 (D.C. Cir. 2001). If an MVPD refuses to offer new programming, customers with access to an alternative MVPD may switch. The FCC shows no reason why this logic does not apply to the cable industry. Indeed, its most recent competition report suggests that it does. According to the Commission, "several very small and rural cable systems have used a variety of schemes to add digital channels, expand their program offerings, and take preemptive action against aggressive DBS marketing." *Seventh Annual Report* ¶ 67.

Given the substantial changes in the cable industry since publication of the *Third Report* in 1999 and our reversal on other grounds, there is little point in our reviewing the Commission's assessment of then-existing market power of cable MVPDs. But whatever conclusions are to be drawn from the new data, it seems clear that in revisiting the horizontal rules the Commission will have to take account of the impact of DBS on that market power. Already when the *Third Report* was written, DBS could be considered to "pass every home in the country." *Third Report*, 14 F.C.C.R. at 19107-08 ¶ 20. The technological and regulatory changes since then appear only to strengthen petitioners' contention. See *Seventh Annual Report* ¶ ¶ 60-82, 140.

With the risk of collusion inadequately substantiated to support the 30% limit and no attempt to find other anticompetitive behavior, there remains the Commission's alternative ground—that programming choices made "unilaterally" by multiple cable companies, *Third Report*, 14 F.C.C.R. at 19118-19 ¶ 51; see also *id.* at 19119 ¶ 53 ("individually"), might reduce a programmer's "open field" below the 40% benchmark. The only support the Commission offered for regulation based on this possibility was the idea that every additional chance for a programmer to secure access would enhance diversity:

> [T]he 30% limit serves the salutary purpose of ensuring that there will be at least 4 MSOs in the marketplace. The rule thus maximizes the potential number of MSOs that will purchase programming. With more MSOs making purchasing decisions, this increases the likelihood that the MSOs will make different

> programming choices and a greater variety of media voices will therefore be available to the public.

Id. ¶ 54. Petitioners challenge the FCC's authority to regulate for this purpose on both constitutional and statutory grounds.

We have some concern how far such a theory may be pressed against First Amendment norms. Everything else being equal, each additional "voice" may be said to enhance diversity. And in this special context, every additional splintering of the cable industry increases the number of *combinations* of companies whose acceptance would in the aggregate lay the foundations for a programmer's viability. But at some point, surely, the marginal value of such an increment in "diversity" would not qualify as an "important" governmental interest. Is moving from 100 possible combinations to 101 "important"? It is not clear to us how a court could determine the point where gaining such an increment is no longer important. And it would be odd to discover that although a newspaper that is the only general daily in a metropolitan area cannot be subjected to a right of reply, see *Miami Herald Publishing Co. v. Tornillo*, 418 U.S. 241 (1974), it could in the name of diversity be forced to self-divide. Certainly the Supreme Court has not gone so far.

We need not face that issue, however, because we conclude that Congress has not given the Commission authority to impose, solely on the basis of the "diversity" precept, a limit that does more than guarantee a programmer two possible outlets (each of them a market adequate for viability). We analyze the agency action under the familiar framework of *Chevron USA, Inc. v. National Resources Defense Council, Inc.*, 467 U.S. 837 (1984). If we find (using traditional tools of statutory interpretation) that Congress has resolved the question, that is the end of the matter. *FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 132 (2000); *National Resources Defense Council, Inc. v. Browner*, 57 F.3d 1122, 1125 (D.C. Cir. 1995). We must place the statutory language in context and "interpret the statute 'as a symmetrical and coherent regulatory scheme.' " *Brown & Williamson*, 529 U.S. at 133.

We begin with the statutory language. The relevant section requires the FCC

> to ensure that no cable operator or group of cable operators can unfairly impede, either because of the size of any individual operator or because of joint actions by a group of operators of sufficient size, the flow of video program-ming from the video programmer to the consumer.

47 U.S.C. § 533(f)(2)(A).

The language addresses only "unfair[ ]" impediments to the flow of programming. The word "unfair" is of course extremely vague. Certainly, the action of several firms that is "joint," in the sense of collusive, may often entail unfairness of a conventional sort. The statute goes further, plainly treating exercise of editorial discretion by a single cable operator as "unfair" simply because that operator is the only game in town. (And *Time Warner I* authoritatively determines that the government is constitutionally entitled to impose limits solely on that ground.) But we cannot see how the word unfair could plausibly apply to the legitimate, independent editorial choices of multiple MSOs. A broad interpretation is plausible *only* for actions that impinge at least to some degree on the interest in competition that lay at the heart of Congress's concern.[6] The Commission's reading of the clause effectively deletes the word "joint" and opens the door to illimitable restrictions in the name of diversity.

Looking at the statute as a whole does little to support the FCC's position. The "interrelated interests" of promoting diversity and fair competition run throughout the 1992 Cable Act's various provi-

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[6]The Commission's economic theory – that cable operators have an incentive to contract with the same programmers in order to lower the programmers' average costs (see discussion in the collusion context, *supra* p. 1152) – would seem to apply regardless of any horizontal limit. Putting various special cases aside, *any* profit-maximizing firm will have an incentive to lower its costs. In a market where a cable operator is a monopolist, the resulting benefit to the firm would be classified as monopoly rents. In a market where an operator is in competition, it can be expected to pass the benefits on to its customers. But the FCC has not shown why such pursuit of lower costs, by the monopolist or the competitive firm, is by itself "unfair," and the statute allows for regulation only if unfairness can be shown.

sions. *Turner II*, 520 U.S. at 189.[7] But despite the duality of interests at work in this section, see *Time Warner I*, 211 F.3d at 1319, it is clear from the structure of the statute that Congress's *primary* concern in authorizing ownership limits is "fair" competition. The statute specifies, after all, that *these* regulations are to be promulgated "[i]n order to enhance effective competition." 47 U.S.C. § 533 (f)(1). In only two of the other sections of the 1992 Cable Act does Congress specify a dominant purpose.[8] This statement of purpose supports a reading that sharply confines the authority to regulate solely in the interest of diversity.

The FCC points to the statutory findings that the "cable industry has become highly concentrated" and that "the potential effects of such concentration are barriers to entry for new programmers and a reduction in the number of media voices available to consumers." *Third Report*, 14 F.C.C.R. at 19118-19 ¶ 51, 1992 Cable Act § 2(a)(4), 106 Stat. at 1460. But reference to a congressional finding cannot overcome the clear language and purpose of the actual provision. The quoted finding stands as little more than support for the proposition that Congress was concerned with the possibilities for market failure and the possible impact on new programmers. The legislative history also offers little. Again, the fact that Congress's interest in anti-competitive behavior may have been animated by an interest in preserving diversity doesn't give the FCC carte blanche to cobble cable operators in the

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[7]The 1992 Cable Act is a wide-ranging statute that includes, besides the ownership limits, must-carry and leased-access requirements, rate regulation, behavioral prohibitions, and privacy protections. See 1992 Cable Act, 106 Stat. 1460.

[8]The leased access provision was amended to add the words "to promote competition in the delivery of diverse sources of video programming" to the section's previously stated purpose of assuring "that the widest possible diversity of information sources are made available." 1992 Cable Act § 9(a), 106 Stat. at 1484; 47 U.S.C. § 532(a). The various behavioral rules designed to prevent cable operators from abusing their market power were passed for the stated purpose of promoting "the public interest, convenience, and necessity by increasing competition and diversity in the multichannel video programming market." 1992 Cable Act § 19, 106 Stat. at 1494; 47 U.S.C. § 547.

name of the latter value alone. After all, Congress also sought to "ensure that cable operators continue to expand, where economically justified, their capacity," 1992 Cable Act § 2(b)(3), 106 Stat. at 1463, and it specifically directed the FCC, in setting the ownership limit, to take into account the "efficiencies and other benefits that might be gained through increased ownership or control." 47 U.S.C. § 533(f)(2)(D).

On the record before us, we conclude that the 30% horizontal limit is in excess of statutory authority. While a 60% limit might be appropriate as necessary to ensure that programmers had an adequate "open field" even in the face of rejection by the largest company, the present record supports no more. In addition, the statute allows the Commission to act prophylactically against the risk of "unfair" conduct by cable operators that might unduly impede the flow of programming, either by the "joint" actions of two or more companies or the independent action of a single company of sufficient size. But the Commission has pointed to nothing in the record supporting a non-conjectural risk of anticompetitive behavior, either by collusion or other means. Accordingly, we reverse and remand with respect to the 30% rule.

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The FCC presents its 40% vertical limit as advancing the same interests invoked in support of its statutory authority to adopt the rule: diversity in programming and fair competition. As with the horizontal rules the FCC must defend the rules themselves under intermediate scrutiny and justify its chosen limit as not burdening substantially more speech than necessary. Far from satisfying this test, the FCC seems to have plucked the 40% limit out of thin air.

The FCC relies almost exclusively on the congressional findings that vertical integration in the cable industry could "make it difficult for non-cable affiliated ... programmers to secure carriage on vertically integrated cable systems" and that "vertically integrated program suppliers have the incentive and the ability to favor their affiliated cable operators ... and program distributors." *Second Report*, 8 F.C.C.R. at 8583 ¶ 41 (citing 1992 Cable Act § 2(a)(5), 106 Stat. at 1460). Regulatory limits in response to these consequences would "increase the

diversity of voices available to the public." *Second Report*, 8 F.C.C.R. at 8583-84 ¶ 42 (citing Senate Report at 80, reprinted in 1991 U.S.C.C.A.N. at 1213). In *Time Warner I* we thought these findings strong enough to overcome the First Amendment challenge to the relevant provision of the 1992 Cable Act. In doing so, we held that such a prophylactic rule was not "rendered unnecessary merely because preexisting statutes [such as the antitrust laws and the antidiscrimination provisions of the 1992 Cable Act] impose behavioral norms." *Time Warner I*, 211 F.3d at 1322-23. Beyond that we did not assess the appropriateness of the burden on speech. We upheld no specific vertical limit—none was before us.

We recognize that in drawing a numerical line an agency will ultimately indulge in some inescapable residue of arbitrariness; even if 40% is a highly justifiable pick, no one could expect the Commission to show why it was materially better than 39% or 41%. See *Missouri Public Service Comm'n v. FERC*, 215 F.3d 1, 5 (D.C. Cir. 2000). But to pass even the arbitrary and capricious standard, the agency must at least reveal " 'a rational connection between the facts found and the choice made.' " *Dickson v. Secretary of Defense*, 68 F.3d 1396, 1404-05 (D.C. Cir. 1995) (quoting *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983). Here the FCC must also meet First Amendment intermediate scrutiny. Yet it appears to provide nothing but the conclusion that "we believe that a 40% limit is appropriate to balance the goals." See *Second Report*, 8 F.C.C.R. at 8593-95 ¶ 68. What are the conditions that make 50% too high and 30% too low? How great is the risk presented by current market conditions? These questions are left unanswered by the Commission's discussion.

The FCC argued before us that no MSO has yet complained that the 40% vertical limit has required it to alter programming. This is no answer at all, as it says nothing about plans that the rule may have scuttled. Petitioners responded that their subsidiaries frequently must juggle their channel lineups to stay within the cap. Furthermore, it appears uncontested that AT&T's merger with MediaOne brings the vertical limits into play. See *In the Matter of Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations from*

MediaOne Group, Inc. to AT&T Corporation, 15 F.C.C.R. 9816 (2000).

In fairness, the FCC does make an attempt to review some relevant conditions. See *Second Report*, 8 F.C.C.R. at 8583-85 ¶ ¶ 41-45. The FCC cites the House Report's conclusion that "some" vertically integrated MSOs favor their affiliates and "may" discriminate against others. *Id.* at 8583-84 ¶ 42 (citing House Report at 43). But it also notes a report that none of the top five MSOs "showed a pattern" of favoring their affiliates. *Id.* at 8584 ¶ 43. Indeed, the FCC concludes that "vertical relationships had increased both the quality and quantity of cable programming services." *Id.* ¶ 44. But still it settled on a limit of 40%. There is no effort to link the numerical limits to the benefits and detriments depicted. Further, given the pursuit of diversity, one might expect some inquiry into whether innovative independent originators of programming find greater success selling to affiliated or to unaffiliated programming firms, but there is none.

Quite apart from the numerical limit vel non, petitioners attack the Commission's refusal to exclude from the vertical limit cable operators that are subject to effective competition. The FCC had proposed exempting cable operators who met the definition of effective competition provided by § 623 of the Communications Act of 1934. See *Implementation of Sections 11 and 13 of the Cable Television Consumer Protection and Competition Act of 1992*, 8 F.C.C.R. 6828, 6862 ¶ 231 (1993) ("First Report"); see also 47 U.S.C. § 543(*l*)(1) (defining the categories of cable operators that are not subject to rate regulation under that section).[9] Of course our decision in *Time Warner I* acknowledged the

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[9]The term "effective competition" means that—

(A) fewer than 30 percent of the households in the franchise area subscribe to the cable system;(B) the franchise area is—

(i) served by at least two unaffiliated multichannel video programming distributors each of which offers comparable video programming to at least 50 percent of the households in the franchise area; and

(ii) the number of households subscribing to programming services offered by multichannel video programming distributors other than the largest multichannel video programming distributor exceeds 15 percent of the households in the franchise area; or

existence of incentives to use affiliated programming. 211 F.3d at 1322. For example, even where an unaffiliated supplier offered a better cost quality trade-off, a company might be reluctant to ditch or curtail an inefficient in-house operation because of the impact on firm executives or other employees, or the resulting spotlight on management's earlier judgment. But petitioners argue, quite plausibly, that exposure to competition will have an impact on a cable company's *ability* to indulge in favoritism for in-house productions. After all, while reliance on inhouse suppliers offering an inferior price-quality trade-off will reduce a monopolist's profits, it may threaten a competitive firm's very survival. This analysis is not foreign to the Commission, which endorsed it when proposing the exemption:

> We believe that this proposal is appropriate since effective competition will preclude cable operators from exercising the market power which originally justified channel occupancy limits. Where systems face effective competition, their incentive to favor an affiliated programmer will be replaced by the incentive to provide programming that is most valued by subscribers. *First Report*, 8 F.C.C.R. at 6862 ¶ 231.

The FCC makes two arguments to justify its refusal to exempt MVPDs that are subject to effective competition. First, it says that the definition of competition provided by 47 U.S.C. § 543 was "not adopted for this specific purpose" but rather for relief from rate regulation. See *Reconsideration Order* 10 F.C.C.R. at 7379 ¶ 47. Indeed, we have recog-

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(C) a multichannel video programming distributor operated by the franchising authority for that franchise area offers video programming to at least 50 percent of the households in that franchise area; or

(D) a local exchange carrier or its affiliate (or any multichannel video programming distributor using the facilities of such carrier or its affiliate) offers video programming services ... in the franchise area of an unaffiliated cable operator which is providing cable service in that franchise area, but only if the video programming services so offered in that area are comparable to the video programming services provided by the unaffiliated cable operator in that area.

47 U.S.C. § 543(*l*)(1).

nized that one of the ways in which the statutory standard is met may be surprisingly defective as a mark of real competition. See *Time Warner Entertainment Co., L.P. v. Federal Communications Commission*, 56 F.3d 151, 166 (D.C. Cir. 1995) (MVPDs satisfying subsection (A) of 47 U.S.C. § 543(*l*)(1) (low penetration) may do so more as a result of geography than competition). But the Commission is free to carve out subsections that are truly pertinent to competition, as it had proposed. See *First Report*, 8 F.C.C.R. at 8662-63 ¶ 232; *Second Report*, 8 F.C.C.R. at 8602 ¶ 85.

Of course competition that is adequate to justify dispensing with rate regulation could still leave an undue likelihood of improper favoritism for affiliated programmers. But the possible failure of readily available criteria does not itself justify the use of so blunt a blade. Congress expressly directed the Commission to take "*particular* account of the market structure..., including the nature and market power of the local franchise." 47 U.S.C. § 533(f)(2)(C) (emphasis added). Because competition raises the stakes for a firm that sacrifices the optimal price-quality trade-off in its acquisition of programming, the issue seems to trigger the legislative directive. Yet the Commission seems to ignore its own conclusions about cable companies' incentives and constraints, and the dynamics of the programming industry. See *First Report*, 8 F.C.C.R. at 6862 ¶ 231. If the criteria of § 543(*l*)(1) are unsuitable, the Commission can consider concepts of effective competition that it finds more apt for these purposes.

Second, the FCC comments that if a competing MVPD favored *its* own affiliated programmers, the presence of competition would have no tendency to create room for independent programmers. See *Reconsideration Order* 10 F.C.C.R at 7379 ¶ 47. But this theory seems contradicted by the Commission's own observation, mentioned earlier, that no vertically integrated MPVD has complained of reaching the 40% limit. Vertically integrated MVPDs evidently use loads of independent programming. Further, although cable operators continue to expand their interests in programmers, "[t]he *proportion* of vertically integrated channels ... continue[d] to decline" for each of the last two years. *Sixth Annual Report*, 15 F.C.C.R. at 1058-59 ¶ 181, *Seventh Annual*

Report ¶ 173 (emphasis added). Even if competing MSOs filled all of their channels with affiliates' products (as unlikely as that seems), the Commission nowhere explains why, in the pursuit of diversity, the independence of competing vertically integrated MVPDs is inferior to the independence of unaffiliated programmers. In any event, the Commission's point here does not respond to the intuition that competition spurs a firm's search for the best price-quality trade-off.

In its brief the Commission adds the argument that truly effective competition under § 543(*l*)(1) existed only for a tiny fraction of cable systems. Indeed, it said in its *Sixth Annual Report* that of the nation's 33,000 cable community units, only 157 satisfy the definition through being in a market offering more than one wireline MVPD. *Sixth Annual Report*, 15 F.C.C.R. at 1045-46 ¶ 142. (In the *Seventh Annual Report* we learn that now 330, or 1% of the total, meet the competition standard through exposure to another MVPD; in this report the qualifier "wireline" is absent. See *Seventh Annual Report* ¶ 138.) But in determining whether or not the regulations burden substantially more speech than necessary, it is a weak move to point to the paucity of MVPDs facing competition if, as seems the case, it is easy to exempt them from the limit.

We find that the FCC has failed to justify its vertical limit as not burdening substantially more speech than necessary. Accordingly, we reverse and remand to the FCC for further consideration.

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We turn, finally, to several aspects of the rules for attributing ownership for purposes of the horizontal and vertical limits, recently revised by the FCC and challenged by petitioners. See *Implementation of the Cable Television Consumer Protection and Competition Act of 1992*, 14 F.C.C.R. 19014 (1999) ("*Attribution Order*"). Petitioners suggest that these rules affect their ability to "speak" to subscribers because of their connection to the horizontal and vertical limits. But petitioners' speech rights are implicated only where their interest allows them to exercise editorial control, in which case attribution would be proper and it is the horizontal or vertical limit that constrains speech. The only effect of the attribution rules where no control is exercised is to limit the

extent of petitioners' investments in a particular class of companies. We therefore review the agency actions under the APA standards, to determine whether they are "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." See 5 U.S.C. § 706(2)(A).

The FCC adopted as its starting point the pre-existing rules for attributing ownership of broadcast television stations, finding that the purposes of the rules are the same. See *Attribution Order*, 14 F.C.C.R. at 19030 ¶ 35; *Second Report* 8 F.C.C.R. at 8577-79, 8593-96 ¶ ¶ 30-35, 56-63. Under that standard, attribution is triggered by ownership of 5% of the voting shares of a company, with various exceptions. See *Attribution of Ownership Interests*, 97 FCC 2d 997 (1984). Because the decisions in the *Attribution Order* tracked, to a large degree, similar decisions related to the broadcast attribution rules, the FCC incorporated by reference much of the reasoning from the broadcast orders. See *Attribution Order*, 14 F.C.C.R. at 19015-16 ¶ 1.

Petitioners challenge the sufficiency and relevance of the Commission's evidence in support of the 5% attribution rule and its failure to adopt an alternative proposed by cable industry interests. They begin by asserting that the FCC improperly relied on two studies that were mentioned neither in the FCC's notice nor in any party's submission. See *Notice of Proposed Rulemaking*, 13 F.C.C.R. 12990 (1998). Although it is true that an agency cannot rest a rule on data " 'that, [in] critical degree, is known only to the agency,' " *Community Nutrition Institute v. Block*, 749 F.2d 50, 57 (D.C. Cir. 1984) (quoting *Portland Cement Ass'n v. Ruckelshaus*, 486 F.2d 375, 393 (D.C. Cir. 1973); see also *International Union, UAW v. OSHA*, 938 F.2d 1310, 1324-35 (D.C. Cir. 1991) (approving reliance on documents not exposed to comment if not "vital" to agency's support for rule), obviously not every cited document is "critical."

Here, although petitioners assert that the studies were the sole evidence cited by the FCC, the Commission also relied on a survey, used to support the 1984 broadcast attribution rules, showing that in widely held corporations, an owner of 5% or more would ordinarily be one of the two or three largest shareholders. See *Attribution Order*, 14 F.C.C.R. at 19034 ¶ 46; *Block*, 749 F.2d at 58 (1984) (new information

"expanded on and confirmed information"). The earlier rulemaking had inferred that with such ownership a holder of 5% or more would be able "to potentially affect the outcome of elective or discretionary decisions and to command the attention of management." *Attribution of Ownership Interests*, 97 FCC 2d at 1005-06 ¶ 14. This hardly seems implausible. Presumably an owner of 5% or more typically has enough of an interest to justify the burden of informing himself about the company's activities and trying to influence (or supplant) management, a fact that management would bear in mind in deciding to whose exhortations it should pay attention. Petitioners have not pointed to any evidence suggesting that the FCC's survey is no longer accurate, or that the conclusion they draw from it has been undermined.

Furthermore, in attacking the relevance of the new studies, the petitioners fail to acknowledge that the FCC sought a rule that would capture "*influence* or control," not just control. *Attribution Order*, 14 F.C.C.R. at 19015-16 ¶ 1 (emphasis added). The Commission specifically noted that a "firm does not need actual operational control over ... a company in order to exert influence." *Id.* at 19030-31 ¶ 36. This distinction also tends to rebut petitioners' critique of the Commission's reliance on the Securities and Exchange Commission's requirement that investors report to the SEC when their holdings exceed 5% of any class of a firm's shares. See 15 U.S.C. § 78m(d)(1). The FCC noted that the purpose of the SEC's requirement was to alert investors to *potential* changes in control, and reasoned that this was similar to its own purpose in the attribution rules, encompassing not merely control but influence. See *Attribution Order*, 14 F.C.C.R. at 19035 ¶ 49 (citing *Securities and Exchange Comm'n v. Savoy Indus., Inc.*, 587 F.2d 1149 (D.C. Cir. 1978)).

Finally, petitioners contend that it was arbitrary for the FCC to reject a "control certification" approach, such as it adopted for partnerships, under which a partner can avoid attribution if (but only if) it certifies to the absence of certain relationships that might betoken control. In this argument, petitioners make a classic apples-and-oranges mix, since the bases that they proposed for self-certification, see *Attribution Order* at 19024 ¶ 22, are quite different

from those adopted by the Commission for partnerships, see *id.* at 19038 ¶ 57 n.163. Even if corporations and partnerships were virtually identical, the Commission would hardly be guilty of self-contradiction if it rejected certification scheme A for corporations and accepted certification scheme B for partnerships. In any event, for corporations the Commission rejected a case-by-case approach on conventional grounds, observing that a bright-line rule was to be preferred because it "reduces regulatory costs, provides regulatory certainty, and permits planning of financial transactions." *Id.* at 19035 ¶ 48; see also *id.* at 19031 ¶ 38. Given an agency's very broad discretion whether to proceed by way of adjudication or rulemaking, see *N.L.R.B. v. Bell Aerospace Co.*, 416 U.S. 267, 294 (1974), and the reasonableness of the 5% criterion, we doubt there was need to explain further. The Commission did, however, observe that the certification proposals offered did "not take into account the variety of ways that an investor may exert influence or control over a company." *Id.* at 19030-31 ¶ 36. And it implicitly distinguished its treatment of partnerships when it said that a limited partner's influence may not be proportional to equity interest "because the extent of its power may be modified by contract." *Id.* at 19039 ¶ 61. Indeed, the Commission's certification rules for partnerships require voting restrictions that would not normally, and perhaps could not, be paralleled in the corporate world (such as abnegation of any power to remove the general partner except under extremely limited circumstances, see *id.* at 19038 ¶ 57 n.163). We find the Commission's discussion adequate.

We also uphold the FCC's adoption of an "equity-and-debt" rule to capture "nonattributable investments that could carry the potential for influence." *Id.* at 19047 ¶ 83. The rule triggers attribution "to an investor that holds an interest that exceeds 33% of the total asset value (equity plus debt) of the applicable entity." *Id.* at 19046-47 ¶ 82.[10]

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[10]The Commission often writes as if investors owned the assets of the companies in which they hold stock or bonds. See, e.g., *Attribution Order*, 14 F.C.C.R. at 19047-48 ¶ 84 n.230. No issue is made here of how its calculations are to be made, e.g., percentage of book value, percentage of market capitalization, or some other method, although

Petitioners attack the sufficiency of evidence to support both the rule itself and the selection of 33% as limit. They observe in particular that the Commission's own claims seem to depend on *combinations* of debt and equity *with* contractual rights. See, e.g., *id.* at 19047 ¶ 83. But the Commission explicitly relied on an earlier rulemaking, see, e.g., *id.* at 19047 ¶ 83, citing *Review of the Commission's Regulations Governing Attribution of Broadcast and Cable/MDS Interests*, 14 F.C.C.R. 12559 (1999) ("Broadcast Attribution Order"), which in turn relied on academic literature, see *id.* at 12589 ¶ 62 nn.132, 134. Petitioners offer no critique of that literature's relevance, and it is not our role to launch one on our own. So we must accept the Commission's basic finding.

Although petitioners independently attack the Commission's selection of 33% as the debt-and-equity limit, we are constrained in our review by the sketchy character of their attack on the basic theory. The Commission's choice of 33% certainly has modest support. It recited the numbers offered by various parties, which ranged from 10% to 50%, in some cases with variations dependent on the presence of special contract provisions. *Attribution Order*, 14 F.C.C.R. at 19048-49 ¶¶ 85-86. Obviously 33% is not far off the median, but, as the Commission says nothing to evaluate the numbers recited, that tells us little.

The Commission also cited its own past decisions, saying that it had used the same percentage for the parallel rule in its broadcast cross-interest policy, and that there it "does not appear to have had a disruptive effect," *id.* at 19048-49 ¶ 86, though without indicating what (if any) assessment it had made. And it referred to two prior adjudications. *Id.* (citing *Cleveland Television Corp.*, 91 FCC 2d 1129 (Rev. Bd. 1982), *aff'd, Cleveland Television Corp. v. Federal Communications Commission*, 732 F.2d 962 (D.C. Cir. 1984), and *Roy M. Speer*, 11 F.C.C.R. 18393 (1996)). In *Cleveland Television* it had simply held that a one-third preferred stock interest conferred " '*in*sufficient incidents of contingent

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the Commission has attempted "clarification" in the broadcast context by allowing applicants to choose their valuation method. See *Review of the Commission's Regulations Governing Attribution of Broadcast and Cable/MDS Interest*, MM Docket No. 94-150, FCC 00-438 (rel. Jan. 19, 2001)¶¶6-28 (2001) ("Attribution Clarification Order").

control' " under various policies, *Attribution Order*, 14 F.C.C.R. at 19048-49 ¶ 86 (emphasis added). In *Roy M. Spear*, it relied on *Cleveland Television* to impose a 33% ownership on a creditor's purchase option, but deferred establishment of any general rule. See 11 F.C.C.R. 18393 ¶ 126 n.26. These prior adjudications provide thin affirmative support for the choice of 33%, though they at least suggest that the Commission has not indulged in self-contradiction. But given the absence of a real probe of the Commission's underlying reasoning for having the restriction at all, the inevitable difficulty in picking such a number, and the deference due the Commission, we cannot find the choice of 33% arbitrary. See *Cassell v. Federal Communications Commission*, 154 F.3d 478, 485 (D.C. Cir. 1998).

Petitioners also challenge the Commission's elimination of an exemption that prevailed in the broadcast attribution rules at the time the cable attribution rules were promulgated. In the broadcast context, an otherwise covered minority shareholder in a company with a single majority shareholder was exempted, on the principle that in such a case the minority shareholder would ordinarily not be able to direct the activities of the company.[11] See *Attribution of Ownership Interests*, 97 FCC 2d at 1008-09 ¶ 21; *Attribution Order*, 14 F.C.C.R. at 19044-46 ¶ ¶ 74-81. There were contentions in the *Broadcast Attribution Order* proceeding that the majority shareholder exemption was being used evasively. See 14 F.C.C.R. at 12574-75 ¶ 29. The Commission neither rejected nor accepted these claims, but retained the exemption. See *id.* at ¶ 36. In dispatching the exemption here, the Commission cited only its concern that a minority shareholder *might* be able to exercise influence even in these circumstances, the "lack of a record ... that the exemption should be retained," and the fact that no one claimed to be using the exemption. *Attribution Order*, 14 F.C.C.R. at 19046 ¶ 81.

The Commission argues here that petitioners lack standing because they have not shown that they are using the exemption.

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[11]The FCC has since eliminated the single majority owner exemption in the broadcast rules to bring it into conformity with the cable rules. See *Attribution Clarification Order* at ¶¶ 41-44.

Again, the FCC disregards the impact the rule can have on investment plans. Petitioners say that they are continually reviewing investment opportunities and that they are constrained by the absence of the single majority exemption. See *supra* p. 20. This is an actual "injury in fact" that is "fairly traceable" to the administrative action. See *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 561 (1992); see also *Committee for Effective Cellular Rules v. Federal Communications Commission*, 53 F.3d 1309, 1315-16 (D.C. Cir. 1995). And of course the absence of current use is no reason to delete an exemption. Removal of the exemption is a tightening of the regulatory screws, if perhaps a minor one. It requires some affirmative justification, cf. *State Farm*, 463 U.S. at 41-42 (requiring justification for removal of a restriction), yet the Commission effectively offers none. Its "concern" about the possibility of influence would be a basis, if supported by some finding grounded in experience or reason, but the Commission made no finding at all. Accordingly, deletion of the exemption cannot stand.

Finally, petitioners object to one of the seven criteria that a cable operator must satisfy in order to be exempt from attribution of limited partnership. The general rule is that *any* partnership interest, no matter how small, leads to attribution, *Attribution Order*, 14 F.C.C.R. at 19039-40 ¶ 61, but a limited partner can secure exemption if it certifies compliance with certain criteria intended to ensure that the partner "will not be materially involved in the media management and operations of the partnership." *Id.* The Commission interprets one of these criteria to bar exemption when a limited partner that is a vertically integrated MSO also sells programming to the partnership. See *id.* at 19055 ¶ 106. This criterion applies even though the limited partner, to achieve exemption, must have certified that it does not "communicate with the licensee or general partners on matters pertaining to the day-to-day operations of its video programming business." *Id.* at 19040-41 ¶ 64.

We agree with petitioners that the no-sale criterion bears no rational relation to the goal, as the Commission has drawn no connection between the sale of programming and the ability of a limited partner to control programming choices. Of course a programmer might secure contract terms giving it some control over a partnership's

programming choices, but, given the independent criterion barring even communications on the video-programming business, see *Attribution Order*, 14 F.C.C.R. at 19040-41 ¶ 64, exercise of that power would seem to be barred. Even if it weren't, the bargaining opportunity would depend on the desirability of the partner's programming, *not* on its status as a partner. The FCC does not even offer a hypothetical to the contrary.

* * *

To summarize, we reverse and remand the horizontal and vertical limits, including the refusal to exempt cable operators subject to effective competition from the vertical limits, for further proceedings. We also reverse and remand the elimination of the majority shareholder exception and the prohibition on sale of programming by an insulated limited partner. We uphold the basic 5% attribution rule and the creation of a 33% equity-and-debt rule.

So ordered

App. 30

United States Court of Appeals
For the District of Columbia Circuit

No. 94-1035 September Term, 2000

Filed On:
UNITED STATES COURT OF APPEALS
FOR DISTRICT OF COLUMBIA CIRCUIT
FILED
MAY 4, 2001
CLERK

Time Warner Entertainment Co., L.P.,
Petitioner

v.

Federal Communications Commission and United States of America,
Respondents

BellSouth Corporation, et al.,
Intervenors

Consolidated with 95-1337, 99-1503, 99-1504, 99-1522, 99-1541, 99-1542, 00-1086,

BEFORE: Edwards, Chief Judge; Williams, Ginsburg, Sentelle, Henderson, Randolph, Rogers, Tatel and Garland, Circuit Judges

ORDER

Upon consideration of intervenors' petition for rehearing en banc, and the absence of a request by any member of the court for a vote, it is

ORDERED that the petition be denied.

Per Curiam

FOR THE COURT
Mark J. Langer, Clerk

BY: s/Robert A. Bonner
Robert A. Bonner
Deputy Clerk

Circuit Judges Henderson and Garland did not participate in this matter.

App. 32
FCC 92-542

IN THE MATTER OF IMPLEMENTATION OF SECTIONS 11 AND 13 OF THE CABLE TELEVISION CONSUMER PROTECTION AND COMPETITION ACT OF 1992 HORIZONTAL AND VERTICAL OWNERSHIP LIMITS, CROSS-OWNERSHIP LIMITATIONS AND ANTI-TRAFFICKING PROVISIONS

MM Docket No. 92-264
Adopted: December 10, 1992; Released: December 28, 1992

NOTICE OF PROPOSED RULE MAKING AND NOTICE OF INQUIRY

Comment Date: February 9, 1993
Reply Comment Date: March 3, 1993
By the Commission:

I. INTRODUCTION

1. On October 5, 1992, Congress enacted the Cable Television Consumer Protection and Competition Act of 1992[1] By this Notice of Proposed Rule Making and Notice of Inquiry ("Notice") we seek comment on the interpretation and implementation of the cross-ownership and anti-trafficking provisions of the 1992 Cable Act. We also seek comment on the adoption of limits on horizontal concentration and vertical integration in the cable industry.

II. BACKGROUND

2. Section 13 of the 1992 Cable Act adds a new Section 617 to the Communications Act of 1934, as *amended*[2] *which establishes a three year*

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[1] Cable Television Consumer Protection and Competition Act of 1992, Pub.L. No. 102-385, 106 Stat. 1460 ("Cable Act of 1992" or "1992 Cable Act").

[2] The Communications Act of 1934, as amended, 47 U.S.C. § 151 et seq. ("Communications Act of 1934").

holding requirement for cable systems. This cable anti-trafficking rule, with certain exceptions, prohibits the sale or transfer of ownership in a cable system within three years following the acquisition or initial construction of such system. Section 11 of the Cable Act of 1992 establishes several restrictions on the ownership and sale of cable systems. First it modifies Section 613(a) of the Communications Act of 1934, as amended, to prohibit the common ownership of a cable system and a multichannel multipoint distribution service ("MMDS") or a cable system and a satellite master antenna television service ("SMATV"), apart from the franchised cable service, within a franchise area. Section 11 of the new Act also amends Section 613 of the Communications Act of 1934 by adding a new subsection (f)(1), which requires the Commission to conduct a proceeding: (1) to prescribe reasonable limits on the number of cable subscribers "a person can reach through cable systems owned by such person ("subscriber limits"); (2) to prescribe reasonable limits on the number of cable channels that can be occupied by a video programmer in which a cable operator has an ownership interest ("channel occupancy limits"); and (3) to consider the necessity and appropriateness of imposing limitations on the degree to which "multichannel video programming distributors" may participate in the creation or production of video programming.

3. The MMDS and SMATV cross-ownership restrictions and the anti-trafficking rule contain no specific effective date and thus, pursuant to Section 28 of the 1992 Cable Act, became effective on December 4, 1992 (the effective date of the 1992 Cable Act). However, the provision of the anti-trafficking rule which limits the amount of time that a franchise authority has to disapprove a request to transfer a cable system, will not become effective until the Commission adopts regulations regarding the information required in connection with such requests.[3] The Cable Act of 1992 also requires the Commission to conduct a proceeding to establish subscriber and channel occupancy limits, and to consider the need for establishing limits on the participation of

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[3] 47 U.S.C. § 537(e).

multichannel video program distributors in the creation and production of video programming, within one year from the date of enactment of the 1992 Cable Act (i.e., by October 5, 1993).

4. Neither the 1992 Cable Act nor its legislative history[4] makes plain Congress' rationale in enacting the anti-trafficking rule. The House Report suggests only that Congress intended this provision to restrict profiteering transactions, which are likely to adversely affect cable rates or service in the franchise area[5] In this proceeding, we seek to identify the proper interpretation of the anti-trafficking rule and to establish an appropriate system of implementation.

5. The 1992 Cable Act and its legislative history demonstrate Congress' concern regarding horizontal concentration and vertical integration in the cable television industry. The vertical and horizontal limits required by Section 11 of the 1992 Cable Act are intended to address these concerns. In particular, Congress sought to prevent large, vertically integrated cable systems from creating barriers to entry for new programmers and from causing a reduction in the number of media voices available to consumers. In addition, the 1992 Cable Act was intended to curb the ability and the incentive of cable operators to favor their affiliated programmers over other programming services. Congress also sought to restrict the degree to which vertically integrated program suppliers favor their affiliated cable operators over unaffiliated cable operators and other program distributors.[6]

6. In drafting the 1992 Cable Act, however, Congress also recognized that certain benefits derive from vertical integration and horizontal

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[4]*See* House Committee on Energy and Commerce, H.R.Rep. No. 102-628 ("House Report"), 102d Cong., 2d Sess. (1992); Senate Committee on Commerce, Science and Transportation, S., Rep. No. 102-92 ("Senate Report"), 102d Cong., 1st Sess. (1991); House Committee on Energy and Commerce, H.R.Conf.Rep. No. 102-862 ("Conference Report"), 102d Cong., 2d Sess. (1992).

[5]The House Report also indicates that the anti-trafficking rule was not meant to prevent lenders from obtaining a security interest in connection with providing financing for cable system acquisitions. House Report at 42.

[6]Cable Act of 1992, Sec. 2.

concentration. For example, the House Report acknowledges that vertical relationships promote diversity and make the creation of new, innovative and risky programming services possible[7] Further, the House Report suggests that vertical relationships may be an efficient way of financing new services and compensating cable operators for assuming some of the risk associated with the launch of new cable programming services.[8] With respect to horizontal concentration, the House Report recognizes that consolidation in the cable industry has benefited consumers by allowing efficiencies in administration, distribution, and programming procurement. Further, the House Committee concluded that large multiple system operators ("MSOs") are able to take risks that small operators would not, and that such MSOs provide a sufficient subscriber base to encourage new program entry.[9] In establishing the subscriber limits and channel occupancy restrictions required by the 1992 Cable Act, the Commission must balance the concerns expressed by Congress with the efficiencies and benefits gained by such increased concentration and integration.

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[7]House Report at 41.

[8]*Id.*

[9]*Id.* at 43.

V. SUBSCRIBER LIMITS

29. Seeking to enhance competition in the development, acquisition and delivery of video programming, Section 11 of the 1992 Act requires the Commission within one year to conduct a proceeding to establish horizontal ownership limits. Specifically, Section 11 requires the Commission to "prescribe reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such person or in which such person has an attributable interest.[42]

30. In establishing subscriber limits, as well as the other ownership limits mandated by Section 11, the 1992 Cable Act directs the Commission to consider the following public interest objectives of the legislation: (A) to ensure that no cable operator or group of cable operators can unfairly impede the flow of video programming from the programmer to the consumer; (B) to ensure that cable operators do not favor affiliated video programmers in determining carriage and do not unreasonably restrict the flow of video programming of unaffiliated video programmers to other video distributors; (C) to take account of the market structure, ownership patterns, and other relationships of the cable industry, including the market power of the local franchise, joint ownership of cable systems and video programmers, and the various types of non- equity controlling interests; (D) to take into account any efficiencies and other benefits that might be gained through increased ownership or control; (E) to ensure that such rules and regulations reflect the dynamic nature of the communications marketplace; (F) to impose limitations that *will not prevent cable operators from serving previously unserved rural areas; and (G) to impose limitations that will not impair the development of diverse and high quality programming.[43] In commenting on the provisions of Section 11, commenters are urged to consider these objectives.

31. The establishment of subscriber limits is intended to address

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[42]47 U.S.C. § 533(f)(1)(A).

[43]47 U.S.C. § 533(f)(2).

Congress' concern regarding increasing horizontal concentration in the cable industry. Horizontal concentration in this context is based on the share of subscribers served by individual cable companies through their ownership or control of local cable systems. The Senate Report noted that TCI, the nation's largest cable operator, serves 14.3 million subscribers (about 24% of the nation's cable subscribers), Time-Warner reaches about 6.4 million subscribers (12% of the nation's subscribers) and the next three largest MSOs, Continental, Comcast and Cox, together control about 5.8 million subscribers (11% of the nation's subscribers).[44] According to information provided to Congress, the top five firms thus serve almost half of the nation's cable subscribers. Congress concluded that this degree of concentration, though low relative to other industries, may enable some MSOs to exercise excessive market power, or monopsony power, in the program acquisition market.[45]

32. In the 1992 Cable Act, Congress found that the increased concentration in the cable industry had the potential to create barriers to entry for new programers and to reduce in the number of media voices available to consumers.[46] Although under traditional antitrust analysis the cable industry is relatively unconcentrated, the 1992 Cable Act requires the Commission to establish limits on the number of subscribers a single entity can reach through cable systems owned by such person.[47] The Conference report is silent regarding what shall consti

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[44]The Committee's statistics are derived from Paul Kagan Associates data and were current as of 1990. More recent data regarding the number of subscribers reached by the 100 largest MSOs can be obtained by reference to Warren Publishing, Inc., Television & Cable Fact Book, Cable & Services Volume No. 59 (Services-Part III), 1992 Edition, p. C-389.

[45]House Report at 42-43.

[46]1992 Cable Act, Section 2(a)(4).

[47]Under the two prevailing measures of market concentration--the four firm concentration ratio ("Four Firm Ratio") and the Hirfindahl-Hirschman Index ("HHI"), the cable industry is not concentrated. The Four Firm Ratio measures the percentage of the

tute reasonable limits for this purpose. The House Report, however, suggests that antitrust analysis should not be the sole measure of concentration in the cable industry.

33. The Commission's own analysis regarding horizontal concentration also concluded that the cable industry has become increasingly concentrated. In its 1990 Report to Congress, the Commission noted that in 1989 the two largest MSOs together served almost 34% of all cable subscribers nationwide, and that the top 10 cable companies served 32.9 million of the nation's 53 million subscribers.[48] We indicated that this degree of concentration among companies that frequently enjoy a monopoly franchise raised "the question of whether MSOs (particularly the largest MSOs) have attained sufficient market power to extract unreasonable concessions from program suppliers and to unfairly restrain competition from alternative distribution services."[49] The Commission also indicated that, on the local level, relatively few cable operators face competition from other multichannel video distributors for either programming or subscribers.[50] In fact, we concluded that it was this level of local concentration that provided MSOs with the potential to take anticompetitive action against programming services

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market captured by the four largest companies in the market. The HHI reflects the distribution of market share among all firms in a given market, giving proportionately greater weight to the market shares of the larger firms. A market is generally considered concentrated when one firm, or a small group of firms, has a sufficient share of the market to exercise power over it. The Justice Department considers an industry concentrated when the HHI exceeds 1800 (although an HHI that exceeds 1000 prompts further evaluation) or when the four firm ratio exceeds 50%. According to the House Report, the HHI for the top 20 MSOs is 491 and the Four Firm ratio for the largest MSOs is 36%, well below the Justice Department's threshold. See House Report at 42.

[48] *Report* in MM Docket No. 89-600, 5 FCCRcd 4962, 5005 (1990) ("1990 Cable Report").

[49] *Id.* at 5003.

[50] *Id.* at 5004.

and competing multichannel providers.[51]

34. On the other hand, the Commission indicated in its 1990 Cable Report that consolidation in the cable industry produced significant benefits and efficiencies to consumers.[52] We noted that higher concentration levels enabled cable companies to take advantage of economies of scale and foster investment in more and better original programming and a wealth of viewing options for consumers. Further, we found that the growth of MSOs had produced significant efficiencies in administration, distribution and procurement of programming which can promote the introduction of new programming services. The Senate Report similarly acknowledged that horizontal concentration may reduce programmers' transaction costs by eliminating the need for negotiation with each of thousands of local cable systems throughout the country.[53] Congress also recognized that horizontal concentration may help promote the introduction of new services into an increasingly competitive programming market by providing capital and a ready subscriber base for such new services.[54]

35. In prescribing subscriber limits, we must, as a preliminary matter, determine the markets in which such subscriber limits should be established. Horizontal concentration may be measured on a local, regional or national basis. The legislative history of the 1992 Cable Act focuses upon the establishment of national subscriber limits, although regional concentration is also mentioned.[55] In the 1990 Cable Report, we concluded that the level of national concentration in the cable

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[51] *Id.* at 5006. In view of our finding in the 1990 Cable Report, we seek comment regarding whether it would be appropriate in calculating compliance with the national subscriber limits to subtract the number of subscribers reached or homes passed by cable systems in areas where effective competition is established.

[52] 1990 *Cable Report* at 5009.

[53] Senate Report at 33.

[54] House Report at 43.

[55] Senate Report at 32-3.

industry was not sufficient to warrant regulatory intervention. We nonetheless indicated that "some cable networks operate on a regional rather than a national basis and an MSO could be sufficiently concentrated to occupy an anticompetitive position at the regional level without possessing a large enough market share to disrupt the national markets."[56] Commenters are asked to indicate whether regional or national subscriber limits, or both, are necessary or appropriate to implement the objectives of the 1992 Cable Act.

36. The Cable Act of 1992 does not define the term "reach" in the context of subscriber limits. Thus, the Commission may prescribe subscriber limits either as a share of cable subscribers or as a share of homes passed. Commenters should address which of these measures should be used to implement the subscriber limits established in this proceeding. We recognize that subscriber-based measures have traditionally been used for purposes of analysis. Nonetheless, we believe that homes passed may be a more appropriate and practical measure for this purpose, since it encompasses all television households for which a particular cable operator provides access to cable programming. Moreover, existing Commission rules applicable to cable/network cross-ownership apply a homes passed measure to implement both national and local subscriber limits.[57] In the Cable/Network Order, we determined that use of a homes passed measure was preferable because a subscriber-based limit could discourage systems from adding new subscribers. We observed that a homes passed measure would be more stable than a subscriber based limit, given the frequent changes in cable subscribership. For the foregoing reasons and to provide consistency in the interpretation of our rules, we tentatively propose to use a homes passed measure to implement

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[56]1990 *Cable Report*, 5 FCCRcd at 5006.A

[57]47 C.F.R. § 76.501 The cable/network restriction was recently relaxed to allow national networks to own cable systems, provided that no such combination exceeds 10% of homes passed by cable nationwide or 50% of homes passed by cable within an ADI. See Report and Order in MM Docket No. 82- 434, 7 FCCRcd 5781 (1992) ("*Cable/Network Order*") (petitions for recon. pending).

the cable subscriber limits established in this proceeding. We seek comment on this proposal.

37. Commenters are also asked to indicate what percentage of homes passed nationally would constitute a reasonable limit on horizontal concentration. Considering the existing market structure and ownership patterns, and the efficiencies and economies of scale resulting from horizontal relationships, we ask whether a limit in the range of 25% to 35% of homes passed would be reasonable or whether some other percentage would be more appropriate. In this regard, commenters should indicate at what percentage of homes passed a single MSO could preclude the success of a new cable service. Are there recent examples of this type of conduct? How many subscribers must be cleared nationally to launch and sustain a new cable programming service? Does the number of subscribers needed vary depending on the type of programming involved? Is it relevant that the Commission's broadcast multiple ownership rules limit the audience reach of television stations in which a person can hold an attributable interest to 25% of television households nationwide.[58] Is it relevant that Commission Rules permit national television networks to own cable systems which reach 10% of the homes passed nationally? This 10% limitation applicable to network-owned cable systems takes into consideration the national audience reach and ability to control programming associated with a broadcast network and, therefore, may not be particularly relevant in the context of crafting national ownership limits for non-network- owned cable systems. It is also important to note that the Senate Report indicates that the 1992 Cable Act was not

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[58]47 C.F.R. § 73.3555. This section also provides for increased ownership of broadcast stations representing up to 30% of the television households nationwide if the additional stations are minority owned. We seek comment on whether we should adopt a similar provision in the cable context. The Commission currently has pending a *Notice of Proposed Rulemaking* in MM Docket No. 91-221 which proposes to relax or eliminate the national audience reach limits applicable to broadcast television. 7 FCCRcd 4111 (1992).

intended to imply that any existing MSO must be divested.[59] Accordingly, commenters are asked to indicate whether divestiture should be required in connection with the subscriber limits we ultimately adopt.

38. The 1992 Cable Act and the Conference Report are silent regarding the appropriate standard for determining ownership of cable systems in connection with application of the subscriber limits. The Senate Report, however, indicates that the Commission should use the attribution criteria set forth in Section 73.3555 (Notes) of our Rules, or such other criteria as the Commission deems appropriate in determining ownership for purposes of applying the subscriber limits.[60] The attribution criteria contained in Section 73.3555 of our Rules may be useful for determining ownership in connection with the subscriber limits we ultimately establish.[61] It should be noted, however, that these attribution criteria were intended to include ownership thresholds which may impart the ability either to influence or control management or programming decisions of a broadcast licensee, and consequently these criteria may not be appropriate to address the concerns at issue in this proceeding. We seek comment regarding whether these attribution criteria (or a modified version thereof) are appropriate for implementing cable subscriber limits or whether some other attribution criteria would be more suitable. In this regard, commenters should also indicate if there are other types of ownership interests, such as non-equity interests, that should be cognizable for purposes of determining ownership under this provision.

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[59]Senate Report at 34. According to the recent data from Warren Publishing, Inc., Television & Cable Fact Book, Cable & Services Volume No. 59 (Services-Part III), 1992 Edition, p. C-389, TCI, the nation's largest MSO, currently reaches 24% of homes passed nationally, and thus it appears that divestiture would not be required if the limit set is within our suggested range of 25% to 30% of homes passed (or higher).

[60]Senate Report at 80.

[61]In the event that we increase the attribution threshold or otherwise modify the attribution criteria as proposed in the Capital Formation Proceeding, commenters should indicate whether we should similarly modify those criteria for purposes of the cable ownership rules.

39. *Jurisdiction and Enforcement.* The 1992 Cable Act does not specifically address how subscriber limits are to be monitored and enforced. In considering this issue it is important to note that presently few if any cable systems are in the range of the proposed subscriber limits. Moreover, subscriber information is publicly available from numerous sources. Consequently, we tentatively conclude that reporting requirements may be unnecessary in connection with enforcing the subscriber limits we ultimately adopt. In the alternative, we believe that a system of certification would be an appropriate means of enforcing the subscriber limits imposed. For example, we could propose requiring cable operators upon transfer or assignment of a cable system to certify that such transfer will not result in ownership of cable systems exceeding the subscriber limits established by the Commission. We seek comment regarding whether such a certification should be made to the local franchise authority, having jurisdiction over the cable system being acquired, or to the Commission. If a system of certification is appropriate, we request comment on whether all cable systems should be required to make the requisite certification or only the five or ten largest cable systems. We also request comment on whether such a certification is necessary at all. Alternatively, we may enforce the subscriber limits on a complaint only basis, pursuant to which parties believing that a particular acquisition would result in a violation of the subscriber limits, would notify the local franchise authority of the acquiring station of the potential violation. We seek comment on these proposals and ask commenters to indicate if there are other more appropriate procedures to enforce the subscriber limits. We also seek comment on whether waivers or exceptions to the subscriber limits should be obtainable in appropriate circumstances. For example, should waivers be granted allowing additional ownership interests for cable systems that expand existing systems to previously unserved rural areas?

40. The Senate Report states that because the cable market is dynamic, the Commission should revisit these limitations at appropriate times to ensure that they continue to accurately reflect the objectives of the

legislation.[62] We believe that periodic review of the ownership limits is important to the continued growth and development of the cable industry. Consequently, we propose to institute a review of the subscriber limits every five years to determine whether such limits are reasonable under the prevailing market conditions. Commenters are asked to indicate whether such review procedures are adequate to ensure that subscriber limits continue to serve the objectives for which they were established.

VI. CHANNEL OCCUPANCY LIMITS

41. Section 11 of the 1992 Cable Act requires the Commission within one year to "prescribe reasonable limits on the number of channels on a cable system that can be occupied by a video programmer in which a cable operator has an attributable interest."[63] Vertical integration in this context refers to common ownership of both cable systems and program networks, channels, services or production companies.

42. In the 1992 Cable Act, Congress concluded that the cable industry has become vertically integrated and that cable operators have the ability and the incentive to favor their affiliated programmers. Such concentration, Congress determined, could make it difficult for non-cable affiliated programmers to secure carriage on cable systems.[64] Similarly, Congress found that, vertically integrated program suppliers also have the incentive and the ability to favor their affiliated cable operators over nonaffiliated operators and program distributors using other technologies.[65] The Senate Report noted that Viacom owns programming services such as MTV, Showtime and Nickelodeon, and that TCI has financial interests in American Movie Classics, the Discovery Channel, QVC and Encore.[66] In addition, the House Report stated

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[62] *Id.* at 80.

[63] 47 U.S.C. § 533(f)(1)(B).

[64] Cable Act of 1992, Section 2(a)(5).

[65] *Id.*

[66] Senate Report at 25.

that according to a study by the National Cable Television Association, 39 of the 68 nationally delivered cable video networks have some ownership affiliation with the operating side of the cable industry.[67]

43. With respect to channel occupancy limits, Congress sought to reduce the incentive and ability of cable operators to favor their affiliated programming services to the disadvantage of unaffiliated programmers. Similarly, Congress intended to discourage vertically integrated programming services from favoring their affiliated cable operators over other cable operators and multichannel video providers. According to the House Report, some vertically integrated MSOs favor programming services in which they have an ownership interest, denying system access to programmers affiliated with rival MSOs. Such vertically integrated MSOs may also discriminate against rival programming services with regard to price, channel positioning, and promotion.[68] In addition, Congress was concerned that vertical integration limits diversity of cable programming and reduces the number of voices available to the public. In this respect, the Senate Report likens the channel occupancy limits to the Commission's broadcast one-to-a-market rule, which are similarly designed to increase the diversity of voices available to the public.[69]

44. On the other hand, the House Report cites a 1988 study by the National Telecommunications and Information Administration ("NTIA"), which concluded that common ownership of cable systems and cable programming services did not appear to affect adversely the supply of cable programming or diversity of viewing choices for cable subscribers.[70] NTIA found that none of the top five MSOs showed a

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[67]House Report at 41.

[68]*Id.* at 43.

[69]Senate Report at 80. The one-to-a-market rule is contained in Section 73.3555 of the Commission's Rules.

[70]House Report at 41, citing *Video Program Distribution and Cable Television: Current Policy Issues and Recommendations*, NTIA Report 88-223, June 1988, p. 102.

pattern of favoring basic services with which they were affiliated. Congress also acknowledged that significant benefits have resulted from vertical relationships in the cable industry. In particular, Congress cited C-Span, CNN, Black Entertainment Television, Nickelodeon, and the Discovery Channel as examples of innovative programming that would not have been feasible without the financial support of cable system operators.[71]

45. In preparing the 1990 Cable Report, we requested and obtained data from nine of the major MSOs regarding the nature and degree of their attributable ownership interests in cable programming services. The data we obtained were current as of December 31, 1989, and are contained in Appendix G to the *1990 Cable Report*.[72] In the 1990 Cable Report, we indicated that TCI owned equity interests in 22 cable networks, Time Warner held interests in eight cable networks and Cox Cable had equity interests in six cable programming services.[73] Overall, we found that MSOs had equity interests in 13 of the top 20 national basic cable networks and in six of the top eight pay cable networks.[74] We concluded that vertical integration had accelerated in the cable industry, but that such vertical relationships had increased both the quality and quantity of cable programming services. We found that MSO investment was responsible for the development and survival of many of the most popular programming services. We also determined that vertical integration of MSOs with significant subscribership has contributed to program diversity by providing new programming services with financial support, an extensive subscriber base and information regarding viewer taste and desire for new programming.

46. The 1992 Cable Act does not indicate the ownership standard that

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[71] *Id.*

[72] *Id.* at 5106-5127.

[73] *1990 Cable Report*, 5 FCCRcd at 5007.

[74] *Id.*

should be applied in connection with channel occupancy limits. The Senate Report indicates that the Committee intended for the Commission to use the attribution criteria set forth in Section 73.3555, or such other criteria as the Commission may deem appropriate in implementing channel occupancy limits. We request comment on whether the attribution criteria contained in Section 73.3555 of our Rules, which are designed to identify ownership interests that afford influence or control over station operations or programming, are appropriate for this purpose. Commenters should indicate whether any modifications should be made for purposes of determining ownership affiliations between cable operators and program services. Commenters are asked to address how application of these attribution rules would affect investment by cable operators in new cable programming services. Parties also are asked to indicate whether higher attribution thresholds are warranted in connection with this restriction in order to provide cable operators with the flexibility to continue investing in new cable programming services.[75]

47. We seek comment on the procedures that should be used in calculating the cable channel occupancy limits we ultimately adopt. The 1992 Cable Act and its legislative history are unclear on this issue. The Senate Report suggests that the Commission may establish such limits based on the number of activated channels, less the number of over-the-air broadcast channels, public, educational, governmental and leased access channels carried. Under this approach, using a hypothetical 20% channel occupancy limit, a system with 54 channels, 14 of which are over-the-air channels, would have a channel occupancy limit of 8 channels for MSO affiliated programming.[76]

48. Parties are requested to comment on whether the procedures for calculating channel occupancy limits outlined in the Senate Report are

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[75]In the event that we increase the attribution threshold or otherwise modify the attribution criteria as proposed in the Capital Formation proceeding, commenters should indicate whether we should similarly modify those criteria for purposes of the cable ownership rules.

[76]Senate Report at 80.

appropriate and reasonably serve the objectives of the legislation. In addressing this issue, commenters should consider that one of the objectives of vertical ownership limits is to ensure that unaffiliated cable programmers have a reasonable opportunity to gain access to vertically integrated cable systems. In this regard, we question whether it is appropriate to subtract the over-the-air broadcast channels and public, educational, governmental and leased access channels in calculating a system's channel capacity. Broadcast channels contain programming that is competitive with cable programming, and leased access channels provide alternative outlets for unaffiliated video programmers. In addition, the commercial and educational broadcast channels are subject to must-carry requirements, pursuant to Section 4 of the 1992 Cable Act. To the extent that carriage of these signals is mandatory, we question whether it is appropriate for such channels to be subtracted from the total number of channels in calculating channel occupancy limits. We seek comment on how such a procedure would serve the statutory objectives of increasing diversity and expanding the number of cable voices available to consumers. We further seek comment regarding how pay channels, such as HBO, Showtime and pay- per-view channels, should be treated for purposes of calculating the channel occupancy limits, since not all subscribers receive these channels. In addition, what provisions should be made for "multiplexing" of pay channels, where the same programming is shown on several different channels at different times? Commenters should also indicate whether channel occupancy limits apply only to vertically integrated national programming networks, or whether such limits should also apply to vertically integrated regional programming networks.

49. It is also unclear from the statutory language and the legislative history how Congress intended such channel occupancy limits to be applied. For example, it is unclear whether such limits were meant to apply only to video programmers affiliated with the particular cable operator or whether such limits were intended to apply to any cable affiliated video programer. It is similarly unclear if the latter interpretation is used, whether the channel occupancy limit should be applied

so that a total of eight channels could be occupied by all vertically integrated programming combined or whether such a limit should be applied so that the programming of each MSO could occupy up to the maximum of eight channels on such a system. The Senate Report could be read to suggest that the channel occupancy limits should apply to the number of channels that any cable operator can devote to any vertically integrated programming, regardless of whether a programmer is affiliated with that particular cable operator.[77] Commenters are asked to indicate how the channel occupancy limits we ultimately adopt should be applied to most effectively address Congress' concerns.

50. Given the uncertainty surrounding the application of the channel occupancy limits, we believe that the more reasoned approach is to apply such limits only to video programmers affiliated with the particular cable operator. We note that such an interpretation would be consistent with Congress' objectives of increasing diversity and expanding the number of voices available to consumers. Moreover, such an interpretation addresses Congress' goal of reducing the ability and the incentive of cable operators' to favor their own affiliated video programmers. Commenters are asked to indicate whether this proposal is appropriate. In considering this issue, commenters should consider whether vertically integrated programing has an adverse effect on diversity. In this regard, we note that, as discussed in paragraph 45, vertical relationships between cable operators and programming services provide essential investment in the development of new programming and enables program producers to spread the risk of developing new and more innovative program services.

51. We also seek comment on how we should determine what constitutes a reasonable channel occupancy limit. What criteria should be used to establish such limits? Are there other regulatory analogies that would be useful in determining what percentage of a cable system's channels should be occupied by vertically integrated program services? In addressing this issue, commenters are asked to consider the vertical

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[77] *Id.*

relationships and ownership patterns that were reported in Appendix G to the 1990 Cable Report. Commenters are asked to provide relevant information, such as the average number of channels occupied by vertically integrated program services. We also request comment on how the availability of leased access channels should affect the establishment of channel occupancy limits. Commenters are asked to indicate the degree to which vertical integration threatens the ability of rival programming services to obtain cable carriage. We note that our intention is to establish a channel occupancy limit that maximizes the number of voices that are available to cable viewers without impairing the ability or incentive of cable operators to invest in new and existing programming services. In this regard, we note that MSO investment has been essential to the development and continuation of many of the most popular and innovative programming services.

52. We tentatively conclude that we should establish a percentage limit on the number of channels that can be occupied by vertically integrated programming services. We ask commenters to indicate what percentage of cable channels would be most appropriate to prevent competitive abuses without discouraging investment relationships between cable operators and program services. In suggesting the appropriate percentage limit, commenters are asked to consider the other structural and behavioral restrictions included in Sections 12 and 19 of the 1992 Cable Act. These restrictions are similarly designed to prevent the adverse effects of vertical integration. Moreover, commenters should consider the must-carry[78] and leased access requirements[79] applicable to cable systems in commenting on this issue.

53. We also seek comment on what effect emerging technologies such as digital signal compression and fiber optic cable should have on the channel occupancy limits. Currently 64% of subscribers receive between 30 and 53 channels, while 28% of cable subscribers receive 54

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[78] 47 U.S.C. § 534.

[79] 47 U.S.C. § 532.

or more channels.[80] Digital compression technology promises to dramatically expand the capacity of existing cable plant. Time Warner is currently testing a cable system with a 150 channel capacity and TCI recently announced plans to introduce a 500 channel system. We believe that such expanded channel capacity will eliminate the need for channel occupancy limits to ensure diversity and prevent discrimination against unaffiliated programming services. Cable systems with such dramatically expanded capacity will require programming from many different sources in order to program so many additional channels. Thus, we propose to establish a threshold beyond which the channel occupancy limits would no longer be applicable. We ask commenters to indicate the appropriate number of total channels for establishing such a threshold. Pursuant to this proposal, the channel occupancy limits would be applied so that a certain percentage of a system's channels could be occupied by vertically integrated programming up to the threshold number of channels, with no limits applicable for channels in excess of the threshold. We believe that this approach is consistent with the objectives of the 1992 Cable Act--to ensure that the regulations prescribed reflect the dynamic nature of the communications marketplace and do not impair the development of diverse and high quality video programming.[81]

54. Finally, we seek comment on whether channel occupancy limits should be phased out in communities where effective competition has developed. Once effective competition has been established and a cable operator no longer occupies a program access bottleneck position, channel occupancy limits may no longer be necessary or desirable. With such developments, the incentive and ability of a cable system to favor its own programming over unaffiliated programming is diminished, and alternative outlets for programming should be available to the public. In seeking comment on this issue, we ask whether

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[80]Warren Publishing, Inc., Television & Cable Fact Book, Cable & Services Volume No. 59 (Services-Part III), 1991 Edition, p. C-389.

[81]47 U.S.C. § 533(f)(2)(E) and (G).

phasing out channel occupancy limits under these conditions is consistent with Congressional intent. In addition, we ask whether channel occupancy limits should be lifted for any cable system that meets the effective competition criteria, or whether only certain of those criteria would justify removing the limits.

55. *Jurisdiction and Enforcement.* The 1992 Cable Act and its legislative history are silent on the issue of enforcement of the channel occupancy limits. We propose that the local franchise authorities have primary responsibility for enforcement of such limits, since they are most familiar with the channel capacity and programming services carried on the systems within their jurisdiction. Because we seek to minimize the burden imposed on local franchise authorities and cable operators by these restrictions, we propose that such channel occupancy limits should be enforced by certification. Accordingly, cable operators would be required to certify annually to the franchise authority that they are in compliance with the channel occupancy limits ultimately adopted. In order to ensure continuous compliance, cable operators would be obligated to notify the franchise authority within 30 days of any changes during the course of the year which would affect compliance with the channel occupancy restrictions. In addition, a franchise authority would be entitled to request any additional information it reasonably determined to be necessary to establish the accuracy of a system's certification, if such certification was challenged. We believe that such a system of certification is appropriate to enforce the channel occupancy limits and will avoid unduly burdening local franchise authorities and cable operators. We also propose to grandfather any existing vertical relationships which exceed the channel occupancy limits at the time such limits are adopted. We believe that divestiture or deletion of programming in connection with implementation of these channel occupancy limits is not required by the 1992 Act and may result in unnecessary disruption of service to the public. We seek comment on this proposal and on whether these procedures are appropriate to ensure compliance with the channel occupancy limits.

FCC 93-456

IN THE MATTER OF
IMPLEMENTATION OF SECTIONS 11 AND 13 OF THE CABLE TELEVISION CONSUMER
PROTECTION AND COMPETITION ACT OF 1992
HORIZONTAL AND VERTICAL OWNERSHIP LIMITS
MM Docket No. 92-264.

Adopted: September 23, 1993 Released: October 22, 1993

SECOND REPORT AND ORDER

By the Commission: Commissioner Barrett issuing a statement.

I. INTRODUCTION

1. In this Second Report and Order ("Report and Order"), the Commission implements Section 11(c)(2) of the Cable Television Consumer Protection and Competition Act of 1992[1] by prescribing national subscriber limits and limits on the number of channels that can be occupied on a cable system by a video programmer in which the cable operator has an attributable interest ("channel occupancy limits"). The Commission declines at this time to impose limits on the degree to which multichannel video programming distributors may engage in the creation or production of video programming as authorized by Section 11(c)(2)(C) of the 1992 Act.[2]

2. We previously issued a Notice of Proposed Rule Making and Notice of Inquiry in this proceeding which sought comment generally on the objectives and scope of Section 11(c)(2) of the 1992 Cable Act.[3] The Notice also asked commenters to address various issues regarding the level at which subscriber limits and channel occupancy limits would be

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[1]Cable Television Consumer Protection and Competition Act of 1992, Pub.L. No. 102-385, 106 Stat. 1460 ("Cable Act of 1992" or "1992 Cable Act").

[2]47 U.S.C. § 533(f)(1)(C).

[3]Notice of Proposed Rule Making and Notice of Inquiry, 8 FCCRcd 210 (1992) ("Notice"). A list of commenters responding to the Notice is provided in Appendix A. These comments were extensively summarized in the Report and Order and Further Notice of Proposed Rule Making ("Further Notice").

reasonable and the appropriate implementation of such limits. In addition, the Commission questioned whether it was necessary or appropriate to adopt limits on the degree to which multichannel video programming distributors ("multichannel distributors") should be permitted to participate in the creation or production of video programming. The Commission subsequently issued a Report and Order and Further Notice of Proposed Rule Making.[4]("Further Notice"), which sought further comment on specific proposals regarding the adoption and implementation of subscriber limits and channel occupancy limits.

3. In summary, this Report and Order contains the following determinations. The Commission establishes a 30% limit on the number of homes passed nationwide that any one entity can reach through cable systems in which such entity has an attributable interest. Horizontal ownership will be determined for this purpose based on the same criteria used by the Commission in the broadcast context. In addition, to promote a diversity of views the Commission will permit ownership of additional cable systems, up to 35% of homes passed nationwide, provided such systems are minority-controlled. However, in view of the recent federal district court decision holding that the Commission's statutory authority to adopt horizontal ownership limits is unconstitutional, and to avoid potential confusion and uncertainty during the period of judicial review the Commission is staying the effective date of the horizontal ownership rules until final judicial resolution of the District Court's decision.[5]

4. With respect to vertical ownership limits, the Commission adopts a 40% limit on the number of channels that can be occupied on a verti-

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[4]Report and Order and Further Notice of Proposed Rule Making in MM Docket No. 92-264, FCC 93-332, released July 23, 1993, ("Further Notice"). A list of commenters responding to the Further Notice and the references to specific commenters used herein is provided in Appendix B.

[5]See Daniels Cablevision v. United States, No. 92-2292 (D.D.C. released September 16, 1993). The vertical ownership limits adopted pursuant to Section 11, which were upheld by the Court are not stayed and will become effective as set forth in para. 109 infra.

cally integrated cable system by video programmers in which the cable operator has an attributable interest. In order to promote a diversity of views the Commission will allow carriage of vertically integrated programming services on two additional channels, or up to 45% of a system's channel capacity, whichever is greater, provided such video programming services are minority-controlled. Vertical attribution is defined for this purpose by reference to the Commission's broadcast attribution criteria. The channel occupancy limits will apply only up to 75 channels. Channel capacity beyond 75 channels will not be subject to vertical ownership restrictions at the present time.

5. The Commission further concludes that in view of the structural and behavioral restrictions already required under the 1992 Act, additional restrictions on the ability of multichannel distributors to engage in the creation or production of video programming are unwarranted at the present. The Commission believes that at the present time the objectives of such a restriction are fully addressed by the vertical and horizontal ownership limits required by Section 11, as well as by the carriage agreement and program access provisions contained in Section 12, and Section 19 of the 1992 Cable Act.

II. BACKGROUND

6. The 1992 Cable Act and its legislative history demonstrate Congress' concern regarding horizontal concentration and vertical integration in the cable television industry. The vertical and horizontal limits required by Section 11 of the 1992 Cable Act are intended to address these concerns. In particular, Congress sought to prevent large, vertically integrated cable systems from creating barriers to entry for new programmers and from causing a reduction in the number of media voices available to consumers. In addition, the 1992 Cable Act was intended to curb the ability and the incentive of cable operators to favor their affiliated video programmers over unaffiliated or competing video programming services. Congress also sought to restrict the degree to which vertically integrated program suppliers favor their affiliated cable operators over unaffiliated cable operators and other program distribu-

tors.[6]

7. In adopting Section 11 of the 1992 Cable Act, Congress also recognized that certain benefits derive from vertical integration and horizontal concentration. For example, the House Report acknowledges that vertical relationships promote program diversity and make the creation of new and innovative programming services possible.[7] Further, the House Report suggests that vertical relationships may be an efficient way of financing new programming services and compensating cable operators for assuming some of the risk associated with the launch of new cable programming services.[8] With respect to horizontal concentration, the House Report recognized that consolidation in the cable industry has benefited consumers by allowing efficiencies in the administration, distribution, and procurement of programming. The House Committee also noted that horizontal concentration may help promote the introduction of new services into an increasingly competitive programming market by providing capital and a ready subscriber base for such new services.[9] The House Report concluded that large multiple system operators ("MSOs") are able to take risks that small operators are not, and that such MSOs provide a large enough subscriber base to facilitate new program entry.[10] The Senate Report similarly acknowledged that horizontal concentration may reduce programmers' transaction costs by eliminating the need for negotiation with individual local cable systems across the country.[11]

8. Recognizing these conflicting factors, Congress directed the Commission to consider and balance the following public interest objectives

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[6]Cable Act of 1992, Section 2.

[7]House Report at 41.

[8]Id.

[9]Id. at 43.

[10]Id.

[11]Senate Report at 33.

in establishing the ownership limits mandated by Section 11: (A) to ensure that no cable operator or group of cable operators can unfairly impede the flow of video programming from the programmer to the consumer; (B) to ensure that cable operators do not favor affiliated video programmers in determining carriage and do not unreasonably restrict the flow of video programming of affiliated video programmers to other video distributors; (C) to take account of the market structure, ownership patterns, and other relationships of the cable industry, including the market power of the local franchise, joint ownership of cable systems and video programmers, and the various types of non- equity controlling interests; (D) to take into account any efficiencies and other benefits that might be gained through increased ownership or control; (E) to make rules and regulations that reflect the dynamic nature of the communications marketplace; (F) to impose no limitations that prevent cable operators from serving previously unserved rural areas; and (G) to impose no limitations that will impair the development of diverse and high quality programming.[12]

III. SUBSCRIBER LIMITS

A. Background.

9. Section 11 of the 1992 Cable Act amends Section 613 of the Communications Act to require the Commission to prescribe regulations establishing reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such person or in which such person has an attributable interest.[13] The adoption of such ownership limits was meant to address Congress' concerns regarding increasing horizontal concentration in the cable industry.

10. Horizontal concentration in this context is based on the share of subscribers served by individual cable companies through their ownership or control of local cable systems. According to information

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[12]47 U.S.C. § 533(f)(2).

[13]47 U.S.C. § 533(f)(1)(A).

provided to Congress, the top five firms serve almost half of the nation's cable subscribers. Congress concluded that this degree of concentration, though low relative to other industries, may enable some MSOs to exercise excessive market power, or monopsony power, in the program acquisition market.[14] Congress was concerned in particular with preventing large vertically integrated cable systems from creating barriers to entry for new video programmers, and from causing a reduction in the number of media voices available to consumers.[15]

11. Although under traditional antitrust analysis the cable industry is relatively unconcentrated, the 1992 Cable Act requires the Commission to establish limits on horizontal concentration.[16] The Conference Report is silent regarding what shall constitute reasonable limits for this purpose. The House Report, however, indicates that antitrust analysis should not be the sole measure of concentration in the cable industry.[17] The House Report suggests that diversity of information sources can only be assured by imposing limits on the ownership of media outlets that are substantially below those that traditional antitrust analysis would support.

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[14]House Report at 42-43.

[15]1992 Cable Act, Section 2(a)(4).

[16]Under the two prevailing measures of market concentration--the four firm concentration ratio ("Four Firm Ratio") and the Hirfindahl-Hirschman Index ("HHI"), the cable industry is not concentrated. The Four Firm Ratio measures the percentage of the market captured by the four largest companies in the market. The HHI reflects the distribution of market share among all firms in a given market, giving proportionately greater weight to the market shares of the larger firms. A market is generally considered concentrated when one firm, or a small group of firms, has a sufficient share of the market to exercise power over it. The Justice Department considers an industry concentrated when the HHI exceeds 1800 (although an HHI that exceeds 1000 prompts further evaluation) or when the four firm ratio exceeds 50%. According to the House Report, the HHI for the top 20 MSOs is 491 and the Four Firm ratio for the largest MSOs is 36%, well below the Justice Department's threshold. See House Report at 42.

[17]House Report at 42.

12. The Commission's own analysis regarding horizontal concentration also concluded that the cable industry has become increasingly concentrated. In its 1990 Report to Congress, the Commission noted that in 1989 the two largest MSOs together served almost 34% of all cable subscribers nationwide, and that the top 10 cable companies served 32.9 million of the nation's 53 million subscribers.[18] We indicated that this degree of concentration among companies that frequently do not face local competition raised "the question of whether MSOs (particularly the largest MSOs) have attained sufficient market power to extract unreasonable concessions from program suppliers and to unfairly restrain competition from alternative distribution services."[19] The Commission also indicated that, on the local level, relatively few cable operators face competition from other multichannel video distributors for either programming or subscribers.[20] The Commission concluded that it was this level of local concentration that provided MSOs with the potential to take anti-competitive action against video programming services and competing multichannel providers.[21]

13. On the other hand, the Commission indicated in its 1990 Cable Report that consolidation in the cable industry produced significant benefits and efficiencies to consumers.[22] We noted that higher concentration levels enabled cable companies to take advantage of economies of scale and foster investment in more and better original programming and a wealth of viewing options for consumers. Further, the Commission found that the growth of MSOs had produced significant efficiencies in administration, distribution and procurement of programming which can promote the introduction of new video programming

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[18]Report in MM Docket No. 89-600, 5 FCCRcd 4962, 5005 (1990) ("1990 Cable Report").

[19]Id. at 5003.

[20]Id. at 5004.

[21]Id. at 5006.

[22]Id. at 5009.

services.[23] Congress similarly found that such benefits and efficiencies result from increased concentration and instructed the Commission to strike a balance between such benefits and the potential for anti- competitive conduct in determining the appropriate level at which to establish subscriber limits.[24]

B. Applicable Market.

14. Further Notice. In the Further Notice, we proposed to adopt exclusively national subscriber limits and asked commenters to indicate whether national subscriber limits would suffice to implement the objectives of the 1992 Cable Act. With respect to regional limits, we tentatively concluded that the benefits of regional concentration outweigh the potential anti-competitive harm that such concentration may have on the local advertising and programming marketplace. Commenters were asked to address this tentative conclusion.

15. Comments. The majority of commenters addressing this issue favor adoption of exclusively national subscriber limits. Several commenters argue that the 1992 Cable Act does not require or even authorize the Commission to promulgate regional subscriber limits. Moreover, commenters indicate that national limits best serve the objectives of the 1992 Cable Act since most programming distribution occurs on a national, not a regional, basis. These parties add that regional limits would threaten the marketplace efficiencies afforded by regional concentration and would impede the incentive of cable operators to invest in fiberoptic and digital compression technologies that will greatly improve cable service and expand channel capacity. Only INTV supports imposing regional subscriber limits, arguing that such limits are necessary to curb the anti-competitive power of MSOs in local advertising markets.[25] However, numerous commenters respond that

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[23]Id.

[24]House Report at 43; Senate Report at 33.

[25]INTV contends that in markets with only one cable operator, that operator is the conduit for all local advertising and therefore is in the position to dictate local advertis-

there is no evidence that cable operators possess market power in the local advertising or program acquisition markets. These commenters contend that in fact, no such evidence exists because the power of cable operators in these markets continues to lag behind local broadcast stations.[26]

16. Discussion. While we disagree with commenters who assert that the Commission is without authority to adopt regional subscriber limits, we decline to adopt such limits at this time. The Senate Report indicates that even prior to the passage of the 1992 Cable Act the Commission had the necessary authority to adopt horizontal limits at the regional level if it found that such restrictions were warranted.[27] Nevertheless, based on the record in this proceeding and on our interpretation of the 1992 Cable Act, we are persuaded that Congress was primarily concerned with national concentration in the cable industry. While the Senate Report indicates that horizontal concentration "at the regional and national level could present concerns about market power," the Report goes on to say that the FCC is required to establish horizontal ownership limits in order to "address the issue of national concentration in the cable industry.[28] Moreover, Congress' objectives in requiring horizontal ownership limits--to prevent the "concentration of the media in the hands of a few" and to limit the ability of MSOs to exercise undue market power in the program acquisition market--can best be served by

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ing prices, which places other local media (e.g., TV stations) at a considerable disadvantage. INTV Initial Comments at 7-8. In response, cable commenters argue INTV's assertions are disingenuous since data shows that broadcast stations continue to control an overwhelming share of the local advertising market as compared to cable interests. See TCI Initial Reply Comments at 19-20; NCTA Initial Reply Comments at 12-13.

[26]See NCTA Comments at 4-6; Time Warner Comments at 5.

[27]The Senate Report states that "[a]lthough the FCC has the authority to impose horizontal limitations on the cable industry (both national and regional) it has not done so." Senate Report at 34.

[28]Senate Report at 32-34.

the adoption of national subscriber limits. Issues of regional concentration we believe would be better addressed by other provisions of the 1992 Act designed to promote the introduction of competition to established cable franchises.

17. In addition, we find no basis in the record at this point for imposing regional limits that could reduce investment in the development of regional programming, upgraded cable infrastructure and improved customer service. We believe that the potential benefits and efficiencies of regional concentration outweigh any anti-competitive affects in the local programming or advertising marketplace. In fact, the record suggests that cable operators do not possess undue power in the local programming or advertising markets where they face competition from local broadcast stations and other multichannel program distributors. In the absence of record evidence suggesting that any cable operator possesses undue power in the local programming or advertising market, we conclude that it is unnecessary to adopt regional limits at this time.

C. Measurement and Percentage Limitation.

18. Further Notice. The Further Notice proposed to establish subscriber limits as a share of homes passed and sought comment on that proposal. We further proposed to adopt a 25% limit on the number of homes passed by cable systems owned by any one entity, although we continued to seek comment on a limit in the range of 20% to 35% of homes passed. We also asked commenters to indicate whether it would be appropriate in calculating compliance with the subscriber limits to subtract the number of homes passed by cable systems where effective competition--as defined in the 1992 Cable Act--is established. Finally, we asked commenters to address our proposal to allow ownership of additional cable systems, beyond the specified limit, provided such systems are minority-controlled.

19. Comments. All commenters responding to the Further Notice favor measuring the audience reach of cable systems by a homes passed

standard rather than a subscriber-based standard.[29] Most commenters agree that a homes passed standard is more appropriate because a measure based on the number of subscribers is relatively unstable and may have the effect of discouraging subscriber growth.

20. On the issue of establishing a reasonable limit on horizontal concentration, cable commenters continue to advocate a subscriber limit of approximately 30% to 40% of homes passed nationwide.[30] These commenters argue that the record does not support the Commission's proposal to adopt a 25% ownership limit. In addition, these commenters assert that in the absence of empirical evidence that existing levels of concentration afford cable operators undue power in the programming market, the Commission should establish subscriber limits significantly above 25%. NCTA, TCI and Time Warner also support allowing additional investments in cable systems beyond the proposed limit provided such cable systems are minority-controlled.[31] TCI suggests that all investments in minority-controlled cable systems should be exempt in order to encourage MSOs to invest in a large number of minority-controlled cable systems. According to these commenters, such ownership incentives will increase minority ownership of cable systems and promote programming diversity.

21. Cable commenters contend that the record indicates that cable

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[29]See NCTA Comments at 9; Liberty Media Initial Comments at 32; NATOA Comments at 14; Discovery Comments at 8-9; MPAA Comments at 2; INTV Initial Comments at 4; TCI Initial Comments at 28-29. Time Warner continues to advocate its earlier proposal that horizontal limits should be measured as fraction which has (a) as its numerator, the number of cable subscribers served by a particular cable operator; and that has (b) as its denominator, the sum of (i) the number of all cable subscribers nationwide and (ii) the number of subscribers served by other multichannel video programming distributors. However, Time Warner concurs with the Commission's proposal to measure horizontal ownership as a share of homes passed nationwide. Time Warner Comments at 9-10.

[30]See Liberty Media Comments at 9; NCTA Comments at 7-8; TCI Comments at 13-17; Time Warner Comments at 7-8; Discovery Initial Comments at 9.

[31]See NCTA Comments at 9; TCI Comments at 18; Time Warner Comments at 7- 8.

systems with a 30% to 40% share could not preclude the launch or success of new video programming services and that establishing ownership limits below this level will impede the development of new cable technologies. Moreover, cable commenters rely on antitrust principles to argue that MSOs must have at least a 50% market share in order to be regarded as having market power. Cable commenters further assert that the program access, must carry, leased access and rate regulation provisions of the 1992 Cable Act already prevent the abuses Congress was concerned might result from excessive horizontal concentration and therefore the structural limits imposed by subscriber limits need not be overly restrictive. Finally, cable commenters contend that adoption of a 25% limit will stifle investment in new cable programming and the development of new technologies because cable operators will not have adequate advertising revenues and subscriber fees to reinvest.

22. In support of their position that a 30% to 40% subscriber limit is reasonable, cable commenters add that extensive subscriber penetration is not essential to the success of a new programming network. Time Warner, TCI and NCTA observe that many cable programming services have flourished at subscriber penetration levels well below 60%.[32] Therefore, these commenters contend that there is no basis on which to conclude that an MSO with a 30% to 40% market share can impede the success of new video programming services.

23. In contrast to the cable commenters, MPAA continues to advocate

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[32]These commenters note that program networks such as Black Entertainment Television, The Learning Channel, Bravo and Court TV have had achieved success with penetration levels of less than 30% to 40%. See Time Warner Comments at 7-8; TCI Comments at 17; NCTA Comments at 7. In addition, Time Warner notes that The Family Channel, which was launched in 1977 achieved less than 10% penetration of all cable homes by its second year of operation, achieved only 22.1% in its third year, but approached 60% penetration by its sixth year of carriage. Another example provided by Time Warner is Nickelodeon, which achieved only 15.1% penetration in its second year of operation and now enjoys over 90% penetration. Time Warner Initial Comments at 27-28.

a 25% subscriber limit. MPAA argues that a limit of 25% of homes passed is reasonable because it does not require divestiture and would in fact allow most cable operators to expand. MPAA also contends that there are no compelling public interest factors which support a subscriber limit higher than 25%. MPAA asserts that higher levels of concentration are not necessary to induce cable operators to invest in the development of advanced cable technologies, and cites numerous examples of cable companies, with subscriber levels below six percent, who have committed to major investments in the deployment of advanced cable technologies.[33] NATOA similarly supports the 25% limit proposed in the Further Notice, arguing that any higher limit would be inadequate to serve Congress' objectives and would allow cable operators to preclude the success of new or competing video programming services by denying them access to an adequate subscriber base to develop the necessary level of viewership.[34]

24. Discussion. The language of Section 11(C)(2)(A) speaks of establishing limits on "the number of cable subscribers" any one person can reach through cable systems owned by such person. We believe that the term "reach" can be reasonably construed to mean the share of homes passed by a cable operator. Such a measure necessarily encompasses all potential cable subscribers and constitutes a more stable basis on which to impose horizontal limits. Moreover, this interpretation would more adequately reflect a cable operator's potential reach, by encompassing all of the cable homes to which a particular cable operator controls access.[35]

25. In adopting ownership limits we seek to balance two competing

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[33]See MPAA Comments at 3.

[34]See NATOA Comments at 13-14.

[35]The Commission similarly employs a homes passed measure to implement the revised network/cable cross-ownership restrictions. See Second Report and Order in MM Docket No. 82-434 (Elimination of Prohibition on Network Cable Cross-Ownership) 7 FCCRcd 1 (1992).

concerns raised by Congress: on the one hand, the possibility that large horizontally integrated MSOs might have the ability to preclude the launch of new video programming services and on the other hand, the benefits and efficiencies that result from greater horizontal concentration.[36] Based on our consideration of these statutory factors and on the preponderance of the data provided in the record, we conclude that a horizontal ownership limit prohibiting any one entity from having an attributable interest in cable systems that in the aggregate reach more than 30% of cable homes passed nationwide strikes the proper balance. A 30% horizontal ownership limit is generally appropriate to prevent the nation's largest MSOs from gaining enhanced leverage from increased horizontal concentration. Nonetheless, it also ensures that the majority of MSOs continue to expand and benefit from the economies of scale necessary to encourage investment in new video programming services and the deployment of advanced cable technologies.

26. We believe that this 30% limit is reasonable to prevent the types of anti- competitive conduct which concerned Congress, particularly when coupled with the behavioral restrictions contained in Sections 12 and 19 of the 1992 Cable Act, which are similarly intended to prevent cable operators from exercising undue power vis-a-vis video programmers and consumers.[37] Moreover, Sections 4 and 5 require cable operators to carry the signals of local commercial and non-commercial broadcast stations. The vertical ownership limits adopted herein and Section 612 of the Communications Act also require cable systems to make a specified percentage of channels available to unaffiliated programmers,

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[36]See para. 7 supra.

[37]Specifically, the restrictions required by Section 12 are designed to prevent cable operators, as well as other multichannel video program distributors, from requiring a financial interest or exclusive rights in a video programming service as a condition of carriage. In addition, Section 19 of the 1992 Cable Act prohibits vertically integrated cable operators from engaging in unfair or deceptive acts or practices the purpose or effect of which is to hinder significantly or to prevent any multichannel video programming distributor from providing programming to consumers.

which ensures that a diversity of views are presented to cable subscribers. The cumulative effect of these regulations coupled with a horizontal ownership limit of 30% should protect against any one cable system exerting undue power that could prevent the success of new video programming services or "unfairly impede the flow of video programming to the consumer.[38] We also believe that this limit combined with the above mentioned provisions will be appropriate to address the diversity aims which underlie the statutory horizontal ownership provisions. At the same time such a limit will allow the majority of cable operators to expand their system ownership and avail themselves of any efficiencies and other benefits which might be gained through increased ownership or control of cable systems.[39]

27. While we proposed a 25% horizontal ownership limit in the Further Notice, we sought comment on a range of 20% to 35%. In concluding that a 30% limit was reasonable we considered a number of factors including the indication in the legislative history of this provision that Congress did not intend necessarily to require the divestiture of any existing interests.[40] In this regard, the Senate Report states that "[t]he legislation does not imply that any existing company must be divested and gives the FCC flexibility to determine what limits are reasonable."[41] Thus, we determined that in the absence of definitive evidence that

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[38]47 U.S.C. § 533(f)(2)(A).

[39]47 U.S.C. § 533(f)(2)(D).

[40]We note in this regard that the largest existing MSO, TCI, using the attribution standards adopted herein, has an interest in cable systems passing approximately 23.8 million homes or 27% of homes passed nationwide. See TCI submission dated September 22, 1993. This number is larger than the number used for corporate and other reporting requirements because, inter alia, it includes systems in which an "attributable interest" is held rather than systems that are treated as "consolidated for certain corporate and other reporting purposes. Compare, Television Digest, June 7, 1993, p. 4 (TCI and consolidated subsidiaries in which the ownership interest is greater than 50% as of December 31, 1992, pass 17.7 million homes).

[41]Senate Report at 34.

existing levels of ownership are sufficient to impede the entry of new video programmers or have an adverse affect on diversity, existing arrangements should not be disrupted. Based on our review and consideration of the record, we are persuaded that such divestiture is unnecessary. There is ample support in the record for a limit of at least 30%. Moreover, we believe that a 30% limit in conjunction with other provisions of the 1992 Cable Act is reasonable to prevent cable operators from creating barriers to the entry of new video programmers without unduly restricting their ability to reach their desired audience. Such a limit will also enable cable operators to avail themselves of the benefits and efficiencies of horizontal concentration and may provide an incentive for MSO investment in upgraded technology and infrastructure.

28. As we proposed in the Further Notice, in order to encourage a diversity of viewpoints we will allow ownership of additional cable systems reaching up to 35% of cable homes passed, provided such additional cable systems are minority-controlled. The Commission has long supported increased minority participation and ownership in the cable industry, believing that such minority ownership is a significant means of fostering the inclusion of a diversity of views in cable programming.[42] We are convinced that the minority ownership incentive we adopt today in connection with the horizontal ownership limits will be an important means of furthering this goal by encouraging MSO investment in minority-owned cable systems, which in turn will promote additional minority ownership of cable facilities and greater minority participation in the selection of programming. We believe that the increased diversity that this additional minority ownership will encourage outweighs the marginal impact on competition that could result from the increased concentration. Notably, we provide a similar incentive

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[42]See Policy Statement on Minority Ownership of Cable Television Facilities, 52 RR 2d 1469, 1471 (1982) (expanding Commission's tax certificate policy to include sales and exchanges of cable television facilities in order to encourage minority ownership of cable facilities).

in the broadcast context to increase the diversity of programming.[43]

29. We decline to calculate compliance with the national subscriber limits by subtracting the number of homes passed by cable systems in areas where effective competition is established. The statutory provisions and the implementing rules we are adopting focus on ensuring that system operators are constrained in terms of the total share of the market they may occupy in order that no single operator exerts an undue influence, particularly at the national level, on the diversity of programming services available through cable television. The presence of competition in particular markets ameliorates some of the concerns involved and provides members of the public in those markets with the opportunity, through the competitor they select, to influence directly the services offered in those markets. The presence of effective competition in any given system or group of systems does not, however, directly respond to Congress' concern about the exercise of undue control by a single entity at the national level.

D. Horizontal Attribution Standard.

30. Further Notice. In the Further Notice we proposed to adopt the broadcast attribution standard to implement horizontal ownership limits and asked commenters to indicate whether this standard was appropriate. We indicated that since these same attribution criteria are used to implement the broadcast multiple ownership rules and cable cross-ownership rules, which have similar objectives, it would appear that they are also appropriate in the context of cable subscriber limits.

31. Comments. Cable commenters generally advocate an attribution standard based on actual control which they contend is more appropriate in determining the ability of a cable operator to control the programming decisions of a particular system.[44] While these commenters recognize that control may be exerted by less than a majority interest, they nevertheless assert that 5% is far too low a standard. NCTA advocates a 20%

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[43]See 47 C.F.R. § 73.3555(e)(1).

[44]See NCTA Comments at 10-11; Time Warner Comments at 13; Liberty Media Initial Comments at 17.

attribution threshold and Time Warner favors a 25% equity threshold.

32. TCI continues to advocate an attribution standard that would (1) exempt ownership interests under 10% ownership; (2) attribute interests of 50% or more; and (3) prorate interests between 10% and 50% based on the number of subscribers served by the system.[45] Generally, TCI and the other cable commenters oppose adoption of the broadcast attribution criteria in this context arguing that such a strict standard is inappropriate because a 5% interest holder is incapable of influencing a cable system's program choices.[46]

33. On the other hand, MPAA, ABC, E! Entertainment, Turner and BET support the use of the broadcast attribution criteria. Specifically, MPAA observes that these criteria have worked well in the broadcast area and were suggested in the legislative history as the appropriate criteria to used in the cable context.[47]

34. Discussion. We believe that the broadcast attribution criteria contained in Section 73.3555 of the Commission's rules are appropriate to implement the horizontal ownership limits.[48] Pursuant to these criteria, all voting stock interests of 5% or more are attributable. Non-voting stock interests (including most "preferred" stock classes) are not attributable. There are several exceptions to the presumption of attribution created by the 5% benchmark. Most notably there is a single majority shareholder exception, which provides that minority interests

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[45]See TCI Comments at 19-24. TCI would also incorporate a single majority shareholder exception as is used in the broadcast context. Id.

[46]See Time Warner Comments at 13. Time Warner also contends that Congress did not intend for the Commission to adopt such a strict attribution standard, noting that the Senate Report that preceded the 1992 Cable Act mentioned the broadcast standard under Section 73.3555 as a possible model for developing attribution criteria. Id.

[47]See MPAA Comments at 6.

[48]For the sake of convenience, the actual rules now being adopted reference the standards set forth in the notes to Section 76.501 of the rules (cable ownership rules). These are derived from and are not substantively different from those generally referred to as the broadcast attribution rules, i.e., Section 73.3555.

will not be attributed where there is a single 51% shareholder. In addition, the interests of "insulated" limited partners are not attributed.

35. In employing the Section 73.3555 attribution criteria for this purpose, we note that the objectives of the broadcast attribution model are consistent with our goals in establishing ownership standards for subscriber limits. In this regard, the broadcast attribution rules focus on ownership thresholds that enable a broadcast licensee to influence or control management or programming decisions. We believe these same issues are also relevant to addressing the concerns at issue in this proceeding relating to the ability of cable operators to unduly influence the programming marketplace. We also note that the legislative history of the 1992 Cable Act supports the use of the broadcast attribution criteria.[49]

E. Enforcement.

36. Further Notice. The Further Notice asked commenters to address how compliance with the subscriber limits should be monitored and enforced. We indicated that since few cable systems were in the proposed range of 20%-35%, a certification process may be appropriate to enforce such limits. We suggested that cable operators reaching 20% of homes passed could be required upon transfer or assignment of a cable system to certify that the transfer or sale of such system would not violate the subscriber limits. Alternatively, we noted that such certification may be unnecessary if the Commission could monitor horizontal concentration by reference to publicly available information. We asked commenters to indicate what sources are publicly available that would enable the Commission to monitor horizontal concentration according to the number of homes passed by the largest cable systems. We also asked commenters to indicate if the Commission should consider waivers of the subscriber limits in appropriate cases and whether the

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[49]See Senate Report at 80. The Senate Report indicates that the Commission should use the attribution criteria set forth in Section 73.3555 (Notes) of our Rules, or such criteria as the Commission deems appropriate in determining ownership under the subscriber limit regulations.

Commission should periodically review the subscriber limits to determine their continuing relevance.

37. Comments. MPAA and most cable commenters support the proposed system of certification to enforce subscriber limits. NCTA and Time Warner, however, indicate that the Commission need not institute a certification process to enforce the subscriber limits since so few companies are near the proposed limits. NCTA suggests that the Commission can readily obtain information regarding the number of cable homes passed using data from Kagan Associates or Cable Television Financial Data, which are relied upon by the industry for subscriber information according to homes passed. Alternatively, TCI and Liberty Media advocate complaint-based enforcement.

38. Time Warner and NCTA also suggest that the Commission should consider waivers in appropriate cases such as for expansion of service into previously unserved rural areas and for de minimis violations (e.g., when commercial circumstances temporarily place an operator over the limits).[50] In addition, MPAA, Time Warner and NCTA favor the Commission's proposal to review the subscriber limits every five years.[51]

39. Discussion. We conclude that in order to enforce most efficiently and effectively the horizontal ownership limits, we should institute a system of certification. Although public information is available from various sources regarding the number of homes passed by the largest cable operators, such sources generally apply different attribution criteria than the Commission has decided to employ. Therefore, we will require entities holding attributable interests in cable systems reaching 20% or more of homes passed nationwide to certify to the Commission, prior to the acquisition of any additional cable systems, that such acquisition will not result in a violation of the horizontal

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[50] See Time Warner Comments at 14; NCTA Comments at 12-13.

[51] See MPAA Comments at 2 & 6-7; Time Warner Comments at 14; NCTA Comments at 13.

ownership limits adopted herein.[52] Where a transaction will result in a cable operator exceeding the limit, the cable operator must seek either a permanent or temporary waiver from the Commission, which might also include a commitment to divest a sufficient number of systems so as to come into compliance with these ownership limits after the acquisition is completed. The Commission will consider waiver requests only in limited circumstances where an acquisition temporarily places a cable operator over the permissible number of subscribers or where an MSO seeks to expand service into an otherwise unserved rural area.

40. Finally, in view of the fact that the cable television industry is so dynamic and fluid, we believe that periodic review of the ownership limits is necessary. As we proposed in the Further Notice, we plan to review the subscriber limits every five years to determine whether such limits are reasonable under the prevailing market conditions and whether such limits continue to serve the objectives for which they were adopted. We regard such periodic review as ~~an~~ important means of addressing Congress' intent that such rules reflect the "dynamic nature of the communications marketplace."[53]

IV. CHANNEL OCCUPANCY LIMITS

A. Background

41. Section 11 of the 1992 Cable Act also requires the Commission to establish reasonable limits on the number of cable channels that can be occupied by a video programmer in which a cable operator has an attributable interest.[54] Congress adopted this provision to address its concerns that the cable industry has become increasingly vertically integrated and that as a result cable operators have the ability and the

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[52]We contemplate that the MSO whose aggregate attributable interests in cable systems equals or exceeds 20% of homes passed nationwide will be responsible for filing the requisite certification. Thus, if a system in which TCI holds an attributable interest acquires an additional cable system, TCI will be the party responsible for certifying to the Commission that the transaction will not result in a violation of FCC rules.

[53]47 U.S.C. § (f)(2)(E).

[54]47 U.S.C. § 533(f)(1)(B).

incentive to favor their affiliated programmers over unaffiliated or competing distributors. Vertical integration in this context refers to common ownership of both programming and distribution systems. Such integration, Congress determined, could make it difficult for non-cable affiliated or competing programmers to secure carriage on vertically integrated cable systems.[55] Congress similarly found that vertically integrated program suppliers have the incentive and the ability to favor their affiliated cable operators over unaffiliated operators and program distributors using other technologies.[56]

42. According to the House Report, some vertically integrated MSOs favor video programming services in which they have an ownership interest, denying system access to unaffiliated programmers and programmers affiliated with rival MSOs. The House Report also found that such vertically integrated MSOs may discriminate against rival video programming services with regard to price, channel positioning, and promotion.[57] In addition, Congress was concerned that vertical integration limits diversity of cable programming and reduces the number of voices available to the public. In this respect, the Senate Report likens the channel occupancy limits to the Commission's broadcast one-to-a-market rule, which is similarly designed to increase the diversity of voices available to the public.[58]

43. On the other hand, the House Report cites a study by the National Telecommunications and Information Administration ("NTIA"), which concluded that common ownership of cable systems and cable programming services did not appear to affect adversely the supply of cable

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[55]Cable Act of 1992, Section 2(a)(5).

[56]Id.

[57]House Report at 43.

[58]Senate Report at 80. The one-to-a-market rule is contained in Section 73.3555 of the Commission's rules.

programming or diversity of viewing choices for cable subscribers.[59] NTIA found that none of the top five MSOs showed a pattern of favoring basic services with which they were affiliated. Congress also acknowledged that significant benefits have resulted from vertical relationships in the cable industry. In particular, the House Report cited C-Span, CNN, Black Entertainment Television, Nickelodeon, and the Discovery Channel as examples of innovative programming that would not have been feasible without the financial support of cable system operators.[60]

44. In the 1990 Cable Report, the Commission also found that the cable industry had become vertically integrated. In this regard, the Commission observed that MSOs had equity interests in 13 of the top 20 national basic cable networks and in 6 of the top 8 pay cable networks.[61] We concluded that vertical integration had accelerated in the cable industry, but that such vertical relationships had increased both the quality and quantity of cable programming services. We found that MSO investment was responsible for the development and survival of several of the most popular video programming services. We also determined that vertical integration among the largest MSOs had contributed to program diversity by providing new video programming services with an extensive subscriber base and information regarding viewer tastes and desires for new programming.

45. As with the establishment of horizontal ownership limits, we seek to establish channel occupancy limits which strike the proper balance between competing statutory objectives: to ensure that vertically integrated cable operators do not favor affiliated video programmers, or unfairly impede the flow of video programming to cable subscribers, on the one hand and, on the other, to encourage MSOs to continue to

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[59]House Report at 41, citing Video Program Distribution and Cable Television: Current Policy Issues and Recommendations, NTIA Report 88-223, June 1988, p. 102.

[60]House Report at 41.

[61]Cable Report at 5009.

invest in the development of diverse and high quality video programming services.[62] Congress expressly indicated that the Commission should "not impose limitations which would impair the development of diverse and high quality programming."[63]

B. Application of Channel Occupancy Limits.

46. Further Notice. In the Further Notice we indicated that the statutory language and legislative history were unclear regarding how Congress intended such channel occupancy limits to be applied. In particular, we noted that we were uncertain whether Congress intended such limits to apply only to video programmers affiliated with the operator of the particular cable system in question or whether such limits were intended to apply to carriage of all cable affiliated video programming on all cable systems. We also questioned whether in calculating a system's channel capacity we should subtract the number of broadcast, PEG and leased access channels.

47. Given the ambiguity, we proposed to apply such limits only to video programmers affiliated with the particular cable operator. We noted that such an interpretation would be consistent with Congress' objectives of increasing diversity and expanding the number of voices available to consumers. Moreover, we observed that such an interpretation would address Congress' goal of reducing the ability and the incentive of cable operators to favor their affiliated video programmers. We also proposed to include all activated channels including broadcast, PEG and leased access channels in calculating system capacity.

48. Comments. Cable commenters assert that the statutory language and the purpose of the legislation make clear that Congress intended for such limits to apply only to video programming services affiliated with the particular cable operator.[64] According to these parties, cable opera

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[62] See para. 7 supra.

[63] 47 U.S.C. § 533(f)(2)(G).

[64] See NCTA at Comments 13-14; Turner Comments at 6; Cablevision Systems Initial Comments at 10; TCI Initial Comments at 35-36; Time Warner Initial Comments at

tors have no incentive to favor a video programmer affiliated with a rival MSO. Nor do they have the ability to influence the programming content of such unaffiliated video programming services. Several commenters also assert that the establishment of channel occupancy limits raises serious First Amendment concerns that will be exacerbated by an unnecessarily broad application of such limits to carriage of all affiliated video programming services on all cable systems.[65]

49. Most commenters also agree that the Commission should take into account all activated channels, including all broadcast, PEG and leased access channels, in calculating system capacity.[66] These commenters note that such channels provide unaffiliated and diverse programming that is competitive with affiliated programming. According to cable commenters, subtracting broadcast, PEG, and leased access channels is unwarranted as a policy matter and would penalize cable operators who carry the broadest array of broadcast, PEG and leased access channels by reducing the channel base available for carriage of affiliated video programming services.

50. In contrast, NATOA contends that the FCC should subtract all broadcast, PEG and leased access channels in calculating channel

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45-48; IFE Initial Comments at 7-9; Liberty Media Comments at 13; E! Entertainment Initial Commentsat 7; Discovery Comments at 5; and Viacom Comments at 7-8; CIC/CC Initial Comments at 35-37. Commenters cite to language in the Conference Report stating that the Commission shall adopt reasonable limits on the "number of channels that can be occupied by a programmer that is owned by a cable operator or in which the cable operator has an attributable interest." Conference Report at 81 (emphasis added).

[65]See Time Warner Initial Comments at 2; Turner Comments at 4; Viacom Initial Comments at 2-3; NCTA Initial Comments at 24; TCI Initial Comments at 29; CIC/CC Initial Comments at 35; Cablevision Systems Initial Comments at 9-10; Liberty Media Initial Comments at 12, n. 5.

[66]See NCTA Comments at 14; Turner Comments at 5; Viacom Comments at 5-8; Time Warner Initial Comments at 41-42; Discovery Comments at 6; CIC/CC Initial Comments at 39-40; Liberty Media Comments at 13-14; MPAA Comments at 9.

capacity.[67] NATOA maintains that the legislative history indicates that Congress intended such channels to be subtracted prior to application of the channel occupancy limits.[68] NATOA also notes that adherence to this procedure would yield more channel capacity for unaffiliated programmers.[69]

51. Discussion. Section 11(c)(2)(B) requires the Commission to "establish reasonable limits on the number of channels on a cable system that can be occupied by a video programmer in which a cable operator has an attributable interest."[70] The language contained in Section 11(c)(2)(B) of the 1992 Cable Act is not entirely clear because it can also be read as applying to carriage of video programmers affiliated with the particular cable operator or to carriage of any vertically integrated cable programmer on any cable system. However, the Conference Report specifies that such limits shall apply to "the number of channels that can be occupied by a video programmer that is owned by a cable operator or in which the operator has an attributable interest."[71]

52. We thus agree with the majority of commenters who assert that the most logical interpretation of the statutory language is to apply such

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[67]See NATOA Comments at 21. See also INTV Initial Comments at 11;

[68]The Senate Report states in relevant part that

"The intent of this provision is to place reasonable limits on the number of channels that can be occupied by each MSO's programming services. For example, the FCC may conclude that each MSO should control no more than 20 percent of the channels on any cable system, with a minimum of 6 channels being permissible. The FCC should establish these rules based on the number of activated channels less the numbers of over-the-air broadcast signals carried and the number of public, educational and governmental and leased access channels carried. On a system with 54 channels, 14 of which are occupied by over-the-air signals or access channels, the limit then would be eight channels that could be occupied by programming owned by an MSO...." Senate Report at 80.

[69]See NATOA Comments at 7.

[70]47 U.S.C. § 533(f)(1)(B) (emphasis added).

[71]Conference Report at 81 (emphasis added).

limits only to video programmers that are vertically integrated with the particular cable operator in question. We believe that this represents the most reasoned approach given Congress' stated objective of encouraging a diversity of voices and preventing unaffiliated programmers from being denied carriage on vertically integrated cable systems.

53. We agree that cable operators have very little incentive to favor video programming services that are affiliated solely with a rival MSO. Moreover, a vertically integrated cable operator appears to have significantly less power to control the content or distribution of a programming service in which it has no ownership interest. Further, we believe that application of the channel occupancy limits to all vertically integrated programmers, regardless of whether they are affiliated with the particular cable operator, would severely inhibit MSO investment in video programming services, since the mere fact of such MSO investment may restrict carriage of the video programming service on all cable systems. In the absence of significant empirical evidence of existing discriminatory practices, we see no useful purpose in limiting the ability of cable operators to carry programming affiliated with a rival MSO. Such a restriction would be unduly burdensome on MSO investment in cable programming and would be contrary to the purpose of the statute. Moreover, we seek to adopt reasonable carriage limits that will balance both the benefits and concerns associated with vertical integration.

54. With respect to calculating channel capacity, we conclude that all activated channels should be taken into account. We note that cable operators are obligated by the 1992 Cable Act to carry local broadcast and noncommercial educational channels, and are required to reserve channel capacity for lease to unaffiliated programmers. Consequently, we conclude that it would be unreasonable to use such channels to reduce the base of channels available for carriage of vertically integrated programming. We believe that the such an approach would penalize cable operators who carry the broadest array of broadcast channels by decreasing the number of channels available for carriage of vertically integrated programming. In addition, we note that there is precedent for including all channels in the calculation of channel capacity in the

must carry and leased access provisions of the Communications Act, which take into account all activated channels in determining a cable operator's carriage obligations.[72] Moreover, carriage of broadcast, PEG and leased access channels promotes diversity and provides alternative sources of unaffiliated programming to cable subscribers in furtherance of the statutory objectives. In this regard, we disagree with NATOA's argument that the legislative history requires that the Commission subtract all broadcast, PEG and leased access channels prior to application of the channel occupancy limits. The Senate Report language relied upon by NATOA appears to be included merely as an example to illustrate how the Commission may decide to calculate channel occupancy limits and therefore does not prohibit the Commission from adopting an alternative approach if it finds such an approach to be reasonable to promote the legislative objectives. In any event, this language is not included in the statute itself.

55. Finally, we address the arguments advanced by some commenters that the channel occupancy provisions of the 1992 Act violate the First Amendment. At the outset, it should be noted that the Commission has an obligation to execute and enforce the provisions of Section 11 enacted by Congress and therefore is not free to declare an act of Congress unconstitutional.[73] Nevertheless, we believe that the statute is constitutional. We note that Congress, in enacting the cable access provisions under the Cable Communications Policy Act of 1984, P.L. 98-549, and the cable must carry obligations under the 1992 Cable Act, carefully considered the First Amendment rights of cable operators and others and concluded that these provisions were constitutionally permissible as consistent with and in furtherance of the goals of the First

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[72]47 U.S.C. §§ 532, 534.

[73]See Johnson v. Robinson, 415 U.S. 361, 368 (1974) and Meredith Corp. v. FCC, 255 U.S.App.D.C. 22, 31 (D.C.Cir.1987).

Amendment.[74] We believe that the channel occupancy limits provided in Section 11 are generally analogous to the cable access and must carry provisions and, similarly, do not believe that these limits infringe the First Amendment rights of cable operators or others. Moreover, we note that the federal district court in Daniels Cablevision, Inc. v. United States, which struck down the subscriber limit authority in Section 11, upheld other provisions of the 1992 Cable Act in dispute, including the Section 11 channel occupancy limits, as "facially compatible with the First Amendment."[75]

C. Vertical Ownership Attribution Standard.

56. Further Notice. The Further Notice proposed to employ the broadcast attribution criteria for purposes of determining vertical integration in the context of channel occupancy limits. Commenters were asked whether these criteria were appropriate or whether a higher attribution standard would be appropriate to encourage continued MSO investment in cable programming. We also asked commenters to indicate whether a higher equity threshold should be adopted where more than one MSO holds a non-controlling interest in a video programming service.

57. Comments. Commenters addressing this issue propose a variety of vertical integration standards. NCTA and most cable commenters

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[74]See H.R.Rep. No. 934, 98th Cong., 2d Sess. at 31-36 (1984) and H.R.Rep. No. 628, 102d Cong., 2d Sess. 58-67 (1992). Indeed, although subject to further review by the U.S. Supreme Court, the cable must carry provisions of the 1992 Act were recently upheld as constitutional as against First Amendment challenges by cable operators and others. Turner Broadcasting System, Inc. v. FCC, 819 F.Supp. 32 (D.D.C.1993) (three-judge court).

[75]The Court in Daniels Cablevision, Inc. said that "the channel occupancy limits appear unrelated to content" but added:

Whether or not the regulations ultimately promulgated by the Commission will pass constitutional muster under O'Brien/Ward is, of course, at this point unclear.

Slip op. at 13. We believe the specific regulations adopted here would meet the O'Brien/Ward test. See United States v. O'Brien, 391 U.S. 367 (1968) and Ward v. Rock Against Racism, 491 U.S. 781 (1989).

favor an ownership criteria based on control, which they define as either majority voting control or the ability to elect a majority of the board of directors.[76] Discovery argues that if integration is defined as less than control, the regulations should include a behavioral exception which, if satisfied, would exempt affiliated video programming service from attribution.[77]

58. MPAA proposes an attribution threshold of 15% (combined with a lower channel occupancy limit) to implement Section 11. MPAA notes that this standard differs from the attribution criteria they recommend in connection with subscriber limits. However, they believed that such a distinction is warranted by marketplace circumstances. In this regard, MPAA observes that it is common for a large number of cable operators to each take a minority position in a programmer, thus spreading control more widely among operators. According to MPAA, such participation by a number of different MSOs warrants a higher attribution level than is applied in cable system ownership, where one MSO generally controls management and operations decisions, including program selection.[78]

59. TCI suggests a vertical integration criteria, pursuant to which ownership interests below 10% would not be attributable; ownership interests above 50% would be fully attributable; and ownership interests between 10% and 50% would be attributable on a prorated basis. TCI contends that this proposal embodies a clear, workable criteria that is superior to proposals favoring ad hoc disputes over the presence or absence of "control."[79]

60. E! Entertainment, ABC, BET, Turner and GTE, on the other hand,

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[76]See NCTA Comments at 18-19; Time Warner Comments at 31-32; Discovery Initial Comments at 19; CIC/CC Initial Comments at 38; Liberty Media Comments at 18-19; Viewer's Choice Comments at 5; IFE Initial Comments at 10.

[77]See Discovery Initial Comments at 19-20.

[78]See MPAA Comments at 7.

[79]See TCI Comments at 19-24.

support the Commission's proposal to use the Section 73.3555 broadcast attribution standards.[80] GTE argues that the Commission should establish a uniform attribution criteria in this dynamic period of convergence of communications technologies. Turner similarly maintains that the Commission should not apply a more restrictive attribution standard than currently applies to broadcasters.[81]

61. Discussion. Section 11(c)(2)(B) of the 1992 Cable Act does not indicate the appropriate criteria for determining vertical ownership attribution. The Senate Report, however, suggests that in determining what is an attributable interest, the Committee intended that the Commission use the attribution rules set forth in Section 73.3555 (Notes) of the Commission's rules or such other criteria as the Commission deems appropriate.[82] We conclude that the broadcast attribution criteria are appropriate for this purpose.

62. In the context of establishing limits on vertical integration in the cable industry we are concerned with identifying interests in cable programming services that are sufficient to afford influence or control over programming decisions. We also seek to identify interests that might potentially provide cable operators with an incentive to favor an affiliated video programming service over an unaffiliated or competing video programming service. However, we must balance these concerns with the objective of preserving the benefits and efficiencies of vertical integration and encouraging continued MSO investment in new video programming services. The broadcast attribution criteria are appropriate to address these competing concerns. The Section 73.3555 attribution criteria were designed to identify all interests that could potentially

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[80]See ABC Comments at 4; Turner Comments at 5-6; and GTE Comments at 3-5; BET Comments at 4-5; E! Entertainment Comments at 4-6. Alternatively, Rainbow Programming proposes a 10% attribution threshold, which it says will make no material difference in a cable operators ability to influence or control a video programmer. See Rainbow Comments at 5.

[81]See Turner Comments at 5.

[82]Senate Report at 80.

afford influence or control over management or programming decisions, while providing exceptions for interests above 5% if there is no realistic possibility of such interests imparting control. Thus, we conclude that the broadcast attribution criteria are strict enough to identify all interests that afford the potential to exert influence or control over management or programming decisions, yet flexible enough to permit continued MSO investment in new video programming services. Moreover, we believe that interests of 5% or greater may be substantial enough to motivate cable to systems to favor an affiliated programmer over a programmer in which the cable system has no attributable interest.

63. We decline to adopt a higher attribution threshold where more than one MSO holds a noncontrolling interest in a video programming service. Although we recognize that common ownership of a programming service by several MSOs may decrease the ability of any one MSO to assert influence or control over programming decisions, we nonetheless continue to believe that such minority interests may be sufficient to provide cable operators with an incentive to favor an affiliated video programming service over an unaffiliated service.

D. Percentage Limitation.

64. Further Notice. In the Further Notice we proposed a 40% limit on the number of channels that could be occupied by affiliated video programmers. Commenters were asked to indicate whether such a limit would be reasonable and would encourage MSOs to continue to invest in new video programming services. We noted that our intention was to establish a channel occupancy limit that would maximize the number of voices available to cable viewers without impairing the ability or incentive of cable operators to invest in new and existing video programming services.

65. Comments. NCTA and most cable commenters indicate that 40% is a minimally acceptable level at which to establish channel occupancy limits. Most cable commenters argue that the channel occupancy limits must be set high enough to preserve the benefits of vertical integration. In this regard, Discovery and Viacom suggest that a channel occupancy limit of 50% would be reasonable. Given the strict attribution standard

proposed by the Commission most cable commenters emphasize that it is essential that the Commission adopt a high enough channel occupancy limit to avoid impeding program investment and distribution. In addition, several commenters endorse the Commission's proposal to allow carriage of additional vertically integrated video programmers provided such video programmers are minority controlled.[83] These commenters agree that such an ownership incentive will increase minority ownership and promote program diversity.

66. TCI supports the proposed 40% limit but continues to advocate that rather than counting channels, the FCC should implement a system based on bandwidth. According to TCI, such an approach would be more precise and adaptable in the forthcoming era of digital compression. Under TCI's recommended approach, channel occupancy limits would be calculated by counting each 6 MHz segment as a single unit and applying limits on the number of units that could be occupied by vertically integrated programming. TCI submits that such an approach will encourage cable operators to continue to invest in the development of new technologies and innovative program services. TCI's proposal is supported by several other cable commenters.[84]

67. MPAA, NATOA and CFA, on the other hand, favor a 20% channel occupancy limit, stating that such a limit would reduce the risk of MSOs favoring affiliated programmers without inhibiting program investment. MPAA asserts that their proposed attribution threshold of 15% combined with a 20% channel occupancy limit better serves Congress' objectives of encouraging MSO investment in new video programming services, while increasing the channel capacity available to unaffiliated video programmers. MPAA suggests that the Commission's proposed 40% limit could result in many instances in no channels being available

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[83]See NATOA Comments at 10; BET Comments at 2-4; TCI Comments at 32; Turner Comments at 6; E! Entertainment Comments at 5; NCTA Comments at 22.

[84]See Time Warner Comments at 23-25; Turner Comments at 4; Liberty Media Initial Comments at 15-16.

to unaffiliated programmers.[85]

68. Discussion. We conclude that a 40% limit on the number of channels[86] that can be occupied by affiliated video programming services is reasonable to serve Congress' competing objectives in requiring such restrictions.[87] We believe that a 40% limit is appropriate to balance the goals of increasing diversity and reducing the incentive and ability of vertically integrated cable operators to favor their affiliated programming, with the benefits and efficiencies associated with vertical integration.[88] Congress and the Commission have both recognized that there

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[85]According to MPAA, it would be possible under the Commission's proposed 40% limit for a substantial number of 36 channel TCI systems to comply with the proposed rule while carrying no unaffiliated programming networks. MPAA adds that a 54 channel TCI system could comply with the proposed rule by "carrying as few as five unaffiliated programming networks." MPAA Comments at 7-8 (emphasis in original).

[86]We will measure the vertical ownership limits on a per channel basis, using the traditional 6MHz per channel definition. However, given the dynamic state of cable technology, we recognize that it may soon be common for cable operators to provide several channels using a single 6MHz bandwidth segment. Accordingly, as with our other rules we intend to review periodically this definition, and if necessary to make adjustments to ensure that it is consistent with the current state of technology.

[87]In order to calculate the exact number of channels on a vertically integrated cable system that can be devoted to carriage of programming in which the cable operator has an attributable interest parties should round up or down to the nearest decimal point. For example, on a system with 34-36 channels, 14 channels could be occupied by affiliated video programming services and on a system with 54-56 channels, 22 could be devoted to the carriage of affiliated programming services. In addition, where a single channel is shared by affiliated and unaffiliated video programming services, such channel will be counted as an affiliated channel only if the affiliated programming service accounts for 50% or more of the channel's programming time.

[88]We disagree with MPAA's assertion that a 40% limit could result in many instances in no channels being made available to unaffiliated video programmers. First, MPAA's calculation does not take into account the availability of leased access channels to unaffiliated video programmers. Second, MPAA appears to assume that TCI owned systems will drop popular unaffiliated programming services such as ESPN, USA Network and A & E in favor of other less popular affiliated programming services.

are benefits which result from vertical integration. First, MSO investment has produced a wealth of high quality cable programming services. Many of the most popular cable programming services were initiated or sustained with the help of MSO investment. Second, vertical integration between cable operators and video programming services appears to produce efficiencies in the distribution, marketing, and purchase of programming."[89] Third, vertical integration can reduce programming costs, which in turn may reduce subscriber fees and cable rates. Fourth, vertical integration may in certain circumstances foster investment in more innovative and riskier video programming services.

69. Moreover, Congress directed the Commission not to adopt limitations "which would impair the development of diverse and high quality video programming.[90] In this regard, we note that cable operators are already required to reserve a substantial percentage of their channel capacity for carriage of local broadcast and PEG stations.[91] In addition, cable operators are subject to leased access requirements, pursuant to which they may be required to designate an additional 15% of their activated channel capacity for commercial use by programmers unaffiliated with the cable operator.[92] Significantly, the leased access obligations are parallel in purpose to the channel occupancy requirements, since they also obligate cable operators to provide system access to

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The record evidence suggests that such conduct is fairly unlikely. See TCI Reply Comments at 13; Time Warner Reply Comments at 14. Finally, MPAA fails to acknowledge that cable systems carrying the maximum number of broadcast must carry and PEG stations are devoting substantial capacity to the carriage of unaffiliated programming.

[89]See Besen Study (attached to TCI Comments) at 23-24.

[90]47 U.S.C. § 533(f)(2)(G).

[91]Cable operators with more than 12 channels may be required to reserve 33% of their activated channel capacity for local broadcast and PEG channels. See 47 U.S.C. §§ 531, 534, 535.

[92]47 U.S.C. § 532.

unaffiliated video programmers. Thus, cable operators' ability to carry affiliated programming is already significantly curtailed by statutorily mandated carriage obligations.

70. We also note that channel occupancy limits are not the only means by which Congress intended to prevent anti-competitive conduct by vertically integrated MSOs. Sections 12 and 19 of the 1992 Cable Act establish specific behavioral restrictions prohibiting discrimination by vertically integrated cable operators and video programming services. As we indicated above, these provisions impose more narrowly tailored behavioral restraints, specifically prohibiting anti-competitive conduct by vertically integrated cable operators and programmers, while channel occupancy limits impose broader structural constraints, which affect the ability of all cable operators to carry programming in which they have an attributable interest. In addition, the must carry, leased access and PEG requirements imposed by other provisions of the Communications Act help to ensure that a diversity of views is available to cable subscribers. In light of the foregoing, we believe that the channel occupancy limits need not be unduly restrictive in order to prevent the incentive and the ability of cable operators to favor their affiliated programmers or to promote a diversity of views to cable subscribers.

71. In addition, in order to promote the presentation of a diversity of viewpoints on cable we will allow carriage of vertically integrated video programming services, on two additional channels or up to 45% of a cable system's channel capacity, which ever is greater, provided such additional video programming services are minority-controlled. As we indicated above with respect to horizontal ownership limits, the Commission has long recognized that the public interest is enhanced when cable programming reflects a diversity of viewpoints.[93] We believe that allowing such expanded carriage of minority-controlled video programming services will encourage additional MSO investment in minority-owned programming services, which will in turn promote minority

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[93]See para 28 supra, citing, Policy Statement on Minority Ownership of Cable Television Facilities, 52 RR2d 1469 (1982).

ownership of video programming services and increase the diversity of viewpoints presented to cable subscribers. In this regard, we believe that the diversity benefits of such increased minority ownership outweigh the access concerns associated with such an increase in integration. We decline, however, to adopt a similar policy for minority oriented- programming. Although we seek to encourage the presentation of a diversity of viewpoints on cable television including those of minorities, we believe that increasing minority ownership of cable systems and video programming services is the most effective and legally sound means of promoting such diversity.[94]

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[94]See Metro Broadcasting v. FCC, 110 SCt. 2997, 3019 and n. 36 (1990) (noting substantial practical and constitutional difficulties that would be presented by FCC promotion of broadcast program diversity through direct program regulation rather than through structural means such as ownership).

G. Effective Competition.

85. Further Notice. In the Further Notice we observed that once effective competition has been established and a cable operator no longer occupies a program access bottleneck position, channel occupancy limits may no longer be necessary or desirable. Thus, we proposed to phase out channel occupancy limits in communities where effectivecompetition is established. We asked commenters to indicate whether the definition of effective competition for this purpose should include cable systems subscribed to by fewer than 30% of the homes located in the franchise area.

86. Comments. Cable commenters addressing this issue all favored our proposal to phase out channel occupancy restrictions in communities where effective competition has developed.[108] Where effective competition exists, these commenters assert that non-vertically integrated video programmers clearly have alternative outlets for programming. In addition, these commenters indicate that there is no incentive for cable operators to favor their affiliated video programming services over unaffiliated or competing video programming services in a competitive marketplace. According to one cable commenter, maintaining such limits where effective competition is established might hinder competition, by enabling a multichannel video program distributor to carry programming owned by a cable operator that the cable operator would not be permitted to carry.

87. MPAA and NATOA, on the other hand, oppose eliminating channel occupancy limits in communities where effective competition develops. MPAA observes that a competing multichannel distributor may also be vertically integrated and removing channel caps in these instances would result in foreclosure of nonaffiliated programmers from either outlet. Both MPAA and NATOA contend that the effective competition standard relates only to rate regulation and is not relevant to the ability of a vertically integrated cable operator to preclude a

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[108] See NCTA Comments at 24; Liberty Media Comments at 16; Time Warner Comments at 37; TCI Initial Comments at 39; Viacom Initial Comments at 17-18; Turner Comments at 7; Discovery Comments at 5-7.

video programmer from obtaining access to subscribers.

88. Discussion. We conclude that we should not eliminate channel occupancy limits in communities where effective competition exists. Although it is argued that the development of effective competition will preclude cable operators from exercising undue power in these situations, the effective competition standard was not adopted for this specific purpose and it is not clear that the presence of effective competition for any cable system addresses all of the relevant concerns that Congress expressed in enacting Section 11 of the Act. For example, if a programming service is excluded from carriage on a competitive system for reasons related to vertical integration, that service will continue to be disadvantaged, and the diversity and competition objectives of this portion of the Cable Act will be frustrated. Thus, at this time, we are not prepared to say that the presence of "effective competition" is a reasonable basis for removing the channel occupancy caps.

89. Congress has, however, indicated that a primary objective of the Act was to "rely on the marketplace to the maximum extent feasible, to promote the availability to the public of a diversity of views and information" and that the legislation was intended to protect consumer interests in the receipt of cable service "where cable television systems are not subject to effective competition.[109] Thus, as with a number of other aspects of these rules, further analysis as to whether the restrictions might be phased out where effective competition develops will be appropriate as we gain more experience with the rules.

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[109] 1992 Cable Act, Section 2(b).

C. Ordering Clauses.

109. Accordingly, IT IS ORDERED that pursuant to the authority contained Sections 2(a), 4(i) and (j) and 303 of the Communications Act of 1934, as amended, and the Cable Television Protection and Competition Act of 1992, Pub.L. No. 102-385, Part 76 of the Commission's Rules, 47 C.F.R. Part 76, Is AMENDED as set forth in Appendix D below, and will become effective January 10, 1994, subject to approval by the Office of Management and Budget. However, the effective date of the horizontal ownership limits contained in Section 76.503 of the Commission's rules IS STAYED pending final judicial resolution of the District Court decision in Daniels Cablevision v. United States, No. 92- 2292 (D.D.C. released September 16, 1993) holding such rules unconstitutional.

E. Additional Information.

110. For additional information regarding this proceeding, contact Jacqueline Chorney, Mass Media Bureau, (202) 632-6990.

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton

Appendix D

Rule Changes

Part 76 of Title 47 of the Code of Federal Regulations is amended to read as follows:

76--CABLE TELEVISION SERVICE

1. The authority citation for Part 76 continues to read as follows:

Authority: Secs. 2, 3, 4, 301, 303, 307, 308, 309, 48 Stat., as amended, 1064, 1065, 1066, 1081, 1082, 1083, 1084, 1085, 1101; 47 U.S.C. Secs. 152, 153, 154, 301, 303, 307, 308, 309, 532, 533, 535, 542, 543, 552, as amended 106 Stat. 1460.

2. Part 76 is amended by adding Section 76.503 to read as follows:

§ 76.503 National Subscriber Limits

* * * * *

(a) Except as set forth in paragraph (b) of this section no person or entity shall be permitted to reach more than 30% of all homes passed nationwide through cable systems owned by such person or entity or in which such person or entity holds an attributable interest.

(b) Ownership of cable systems reaching up to 35% of all homes passed nationwide shall be permitted provided the additional cable systems, beyond 30% of homes passed nationwide, are minority-controlled.

(c) Prior to acquiring additional cable systems any person or entity holding an attributable interest in cable systems reaching 20%, or more, of homes passed nationwide must certify to the Commission that no violation of the national subscriber limits prescribed in this section will occur as a result of such acquisition.

Note 1: For purposes of this Section:

(a) "Minority-Controlled" means more than 50% owned by one or more members of a minority group.

(b) "Minority" means Black, Hispanic, American Indian, Alaska ative, Asian and Pacific Islander.

(c) "Attributable Interest" shall be defined by reference to the criteria set forth in the Notes to § 76.501.

* * * * *

3. Part 76 is amended by adding Section 76.504 to read as follows:

§ 76.504 Limits on Carriage of Vertically Integrated Programming

(a) Except as otherwise provided in this section no cable operator shall devote more than 40% of its activated channels to the carriage of national video programming services owned by the cable operator or in which the cable operator has an attributable interest.

(b) The channel occupancy limits set forth in paragraph (a) shall apply only to channel capacity up to 75 channels.

(c) A cable operator may devote two additional channels or up to 45% of its channel capacity, whichever is greater, to the carriage of video programming services owned by the cable operator or in which the cable operator has an attributable interest provided such video programming services are minority- controlled.

(d) Cable operators carrying video programming services owned by the cable operator or in which the cable operator holds an attributable interest in excess of limits set forth in paragraph (a) as of December 4, 1992 shall not be precluded by the restrictions in this section.

(e) Cable operators are required to maintain records in their public file for a period of three years regarding the nature and extent of their attributable interests in all video programming services as well as information regarding their carriage of such verticlaly integrated video programming services on cable systems in which they also have an attributable interest. These records must be made available to local franchise authorities, the Commission, or members of the public on reasonable notice and during regular business hours.

Note 1: For purposes of this Section:

(a) "Minority-Controlled" means more than 50% owned by one or more members of a minority group.

(b) "Minority" means Black, Hispanic, American Indian, Alaska Native, Asian and Pacific Islander.

(c) "Attributable Interest" shall be defined by reference to the criteria set forth in the Notes to § 76.501.

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App. 95

SEPARATE STATEMENT OF
COMMISSIONER ANDREW C. BARRETT

RE: Implementation of the Cable Television Consumer Protection and Competition Act of 1992--Cable Ownership

This Second Report and Order adopts regulations regarding horizontal ownership and channel occupancy limits. In particular, the Commission establishes (1) a horizontal limit at 30% of homes passed nationally by cable systems owned by any single entity, with an allowance for ownership of systems totalling an additional 5% beyond the horizontal limit provided that such systems are minority controlled; and (2) a 40%-limit for channels occupied by programming services that are vertically integrated with a particular cable operator, applicable up to 75 channels. Regarding the channel occupancy limit, the rules allow for an additional two channels, or 5% of the cable system's total channels, whichever is greater, provided that the services are minority controlled.

I write separately to emphasize the importance of the horizontal and vertical ownership limits as structural measures addressing the aspects of concentration and vertical integration in the multichannel marketplace. In particular, I am concerned that these measures must be viewed the context of the Commission's prior decisions on rate regulation and program access, as well as the rules adopted today concerning program carriage agreements.[110] Given the existing behavioral regulations imposed on vertically integrated cable operators and programming vendors, these cable ownership provisions will become the

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[110] See Rate Order and Further Notice of Proposed Rule Making, MM Docket No. 92-266, FCC 93-177, released May 3, 1993; 58 Fed.Reg. 29736. See also First Report and Order, MM Docket No. 92-265, 8 FCCRcd 3359 (1993); Second Report and Order, MM Docket No. 92-265, adopted September 23, 1993.

structural component that will govern the cable industry's transition from a regulated environment to effective competition. In this regard, I believe that greater availability of programming services to all distributors will play a critical role in determining whether the future broadband network will ultimately belong to all multichannel competitors, including cable operators, to the extent that they remain able to invest and exercise creativity. Therefore, I am concerned that the channel occupancy rules must incorporate sufficient flexibility to permit future opportunities for investment leading to the development of new ventures and programming.

I am also interested in the higher thresholds established to allow for ownership and channel occupancy where cable systems and programming services are minority controlled. I support these provisions that will promote opportunities for greater participation by minority enterprises in the multichannel marketplace as program vendors and distributors.

Finally, the horizontal ownership provisions are affected by the decision by the United States District court for the District of Columbia regarding the constitutionality of this portion of Section 11 of the 1992 Cable Act.[111] Although the Court has found the statute's numerical limit on subscribers unconstitutional, the decision includes a provision to stay the results pending completion of any proceedings on appeal. Therefore, I am concerned that the Commission will need to monitor the development of this litigation and the ramifications of any further events concerning the effectiveness of the cable ownership rules, especially to the extent that any developments regarding the vertical limits could affect the availability of programming services.

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[111]See Daniels Cablevision v. United States of America, No. 92-2292 [D.D.C., released September 16, 1993].

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of the Cable	)	
Television Consumer Protection	)	CS Docket No. 98-82
and Competition Act of 1992	)	
	)	
Review of the Commission's	)	
Cable Attribution Rules	)	

NOTICE OF PROPOSED RULEMAKING

Adopted: June 4, 1998 Released: June 26, 1998

Comment Date: August 14, 1998

Reply Comment Date: September 3, 1998

By the Commission:

I. INTRODUCTION

1. With this *Notice of Proposed Rulemaking*, we initiate a review of our cable attribution rules, which define what constitutes a "cognizable interest" that triggers application of various Commission rules relating to the provision of cable television services. The attribution rules seek to identify those corporate, financial, partnership, ownership and other business relationships that confer on their holders a degree of ownership or other economic interest, *or* influence or control over an entity engaged in the provision of communications services such that the holders should be subject to the Commission's regulation. We are initiating this rulemaking in light of recent developments in the cable industry, including numerous strategic alliances, partnerships, system swaps, mergers and acquisitions among cable entities; various Commission proceedings related to the issue of cable ownership, such as the cross-ownership proceedings, horizontal ownership proceedings, and biennual review; and the Commission's review, in a separate proceeding, of the broadcast attribution rules on which many of our

cable attribution rules were based.[1] Where appropriate, we provide a brief summary of the attribution issues contained in the *Broadcast Attribution Notice* and *Broadcast Attribution Further Notice*; for a full discussion of these issues, interested parties are directed to review those documents.

II. NOTICE OF PROPOSED RULEMAKING

2. *Background.* The cable attribution rules are particularly significant in the context of a number of statutory provisions enacted as part of the Cable Television Consumer Protection and Competition Act of 1992[2] (the "1992 Cable Act"), including: (1) former Section 613(a)(1), which prohibited the common ownership of local television stations and cable systems that serve the same area (the "cable/broadcast station cross-ownership restriction");[3] (2) Section

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[1] *See Notice of Proposed Rule Making, Review of the Commission's Regulations Governing the Attribution of Mass Media Interests*, MM Docket Nos. 94-150, 92-51 and 87-154, FCC 94-324, 10 FCC Rcd 3606 (1995) ("*Broadcast Attribution Notice*"); *Further Notice of Proposed Rule Making, Regulations Governing Attribution of Broadcast and Cable/MDS Interests, Regulation and Policies Affecting Investment in the Broadcast Industry and Reexamination of the Commission's Cross-Interest Policy*, MM Docket Nos. 94-150, 92-51 and 87-154, FCC 96-436, 11 FCC Rcd 19895 (1996) ("*Broadcast Attribution Further Notice*").

[2] Pub. L. No. 102-385, 106 Stat. 1460 (1992), 47 U.S.C. § 521, *et seq.* (1992).

[3] Section 613(a)(1) of the Communications Act of 1934, as amended (the "Communications Act"), 47 U.S.C. § 533(a)(1) (1992). The cable/broadcast station cross-ownership rule was first adopted by the Commission in 1970 and modified in 1992. *See Second Report and Order, Amendment of Part 74, Subpart K, of the Commission's Rules and Regulations Relative to Community Antenna Television Systems; and Inquiry into the Development of Communications Technology and Services to Formulate Regulatory Policy and Rulemaking and/or Legislative Proposals*, Docket No. 18397, 23 FCC 2d 816 (1970); *Report and Order, Amendment of Part 76, Subpart J, Section 76.501 of the Commission's Rules and Regulations to Eliminate The Prohibition on Common Ownership of Cable Television Systems and National Television Networks*, MM Docket No. 82-434, 7 FCC Rcd 6156, 6174 n.54 (1992); 47 C.F.R. § 76.501. The cable/broadcast station cross-ownership restriction was codified by statute in the Cable Communications Policy Act of 1984, Pub. L. No. 98-549, 98 Stat. 2779 (1984). Although the Telecommunications Act of 1996 eliminated the statutory cable/broadcast station cross-ownership restriction, it left in place the

613(f)(1)(A), which requires the Commission to establish reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such person, or in which such person has an attributable interest ("horizontal cable ownership limits");[4] (3) Section 613(f)(1)(B), which requires the Commission to establish reasonable limits on the number of channels on a cable system that can be occupied by a video programmer in which a cable operator has an attributable interest ("vertical occupancy limits");[5] (4) Section 613(a)(2), which prohibits a cable operator from holding a license to provide multichannel multipoint distribution service ("MMDS"), or from offering satellite master antennae television ("SMATV") service separate and apart from any franchised cable service, in any portion of the franchise area served by the cable operator's cable system (the "cable/MMDS" and "cable/SMATV" cross-ownership restrictions);[6] (5) Section 628, which, among other things, requires the Commission to

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Commission's equivalent rule at 76 C.F.R. § 76.501, pending Commission review of our rules. *See* Section 202(i)(1) of the Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) (the "1996 Act"); *Joint Explanatory Statement of the Committee of Conference, Telecommunications Act of 1996*, S. Rep. 104-230 at 164 (February 1, 1996) ("The conferees do not intend that this repeal of the statutory prohibition should prejudge the outcome of any review by the Commission of its rules.") The 1996 Act also eliminated the prohibition on broadcast television networks' ownership or control of cable systems, and the Commission has amended our rule at 76 C.F.R. § 76.501 to eliminate the prohibition in conformity therewith. *See* 1996 Act, Section 202(f); *Order Implementing Sections 202(f), 202(i) and 301(i) of the Telecommunications Act of 1996*, CS Docket No. 95-56, FCC 96-112, 11 FCC Rcd 15115 (1996).

[4] Communications Act § 613(f)(1)(A), 47 U.S.C. § 533(f)(1)(A).

[5] Communications Act § 613(f)(1)(B), 47 U.S.C. § 533(f)(1)(B).

[6] Communications Act § 613(a)(2), 47 U.S.C. § 533(a)(2) (now Communications Act § 613(a), 47 U.S.C. § 533(a)). The 1996 Act amends this provision to state that it does not apply to any cable operator in any franchise area in which that cable operator faces "effective competition." *See* 1996 Act § 202(i)(6), codified at Communications Act § 613(a)(3), 47 U.S.C. § 533(a)(3), and the Commission's rules implementing this provision
at 47 C.F.R. §§ 21.912(e)(3), 76.501(f).

establish safeguards to prevent a cable operator with an attributable interest in a programming vendor from engaging in unfair or deceptive acts involving the distribution of programming to an unaffiliated multichannel video programming distributor ("program access" rules);[7] and (6) Section 616, which, among other things, restricts the activities of cable operators and other multichannel programming distributors when dealing with programming vendors, including prohibiting discrimination in the selection, terms, or conditions of carriage, on the basis of a vendor's affiliation or non-affiliation ("program carriage" rules).[8] Implementation of the foregoing rules serve two goals: (1) promoting diversity; and (2) deterring anticompetitive practices. As discussed below, for those cable ownership rules implemented to promote competition and diversity, the Commission adopted attribution rules from the broadcast context where the goal is the same. For those rules implemented to deter specific improper practices as well as to promote competition and diversity, the Commission adopted stricter attribution standards.

3. In 1984, the Commission conducted a comprehensive rulemaking proceeding and decided to adopt a single attribution standard for our cross-ownership rules which govern the extent to which a single entity may simultaneously hold ownership interests in

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[7] Communications Act § 628(b), 47 U.S.C. § 548(b). *See also First Report and Order, Implementation of Sections 12 & 19 of the Cable Television Consumer Protection and Competition Act of 1992 -- Development of Competition and Diversity in Video Programming and Distribution and Carriage*, MM Docket 92-265, 8 FCC Rcd 3359, 3370 (1993) ("*Program Access Order*"), *recon. granted in part, Memorandum Opinion and Order on Reconsideration of the First Report and Order*, MM Docket No. 92-265, 10 FCC Rcd 1902 (1994) ("*Mem. Op. on Recon. of Program Access Order*").

[8] Communications Act § 616(a), 47 U.S.C. § 536(a). *See also Second Report and Order, Implementation of Sections 12 and 19 of the Cable Television Consumer Protection and Competition Act of 1992 -- Development of Video Programming Distribution and Carriage*, MM Docket No. 92-265, 9 FCC Rcd 2642, 2643-44 (1993) ("*Program Carriage Order*").

broadcast stations, cable television systems, and newspaper entities.[9] Although we did not perform a separate analysis of the ownership structures of cable systems, we were "reasonably certain" that they were not sufficiently different from broadcasting to justify the adoption of a distinct benchmark.[10] The resulting standard (the "broadcast attribution standard") generally provides that partnership interests, direct ownership interests, and voting stock interests of 5% or more are attributable. For passive investors, the voting stock benchmark is 10%. Non-voting stock interests (including most "preferred" stock classes) are not attributable. There are several exceptions to the voting stock threshold, including a "single majority shareholder" exception, which provides that minority interests will not be attributed where a single shareholder owns more than 50% of the outstanding voting stock. In addition, the interests of "insulated" limited partners are not attributed.[11]

4. In our rulemaking proceedings under the 1992 Cable Act, we determined that the broadcast attribution standard still governs broad structural rules, such as the horizontal cable ownership limits[12] and vertical channel occupancy limits,[13] that are designed to

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9 *See Report and Order, Amendment of the Rules concerning Attribution of Ownership of Broadcast Licensees,* MM Docket No. 83-46, 97 FCC 2d 997, 1032 (1984), *recon. in part, Memorandum Opinion and Order,* MM Docket No. 83-46, FCC 85-252, 58 RR 2d 604 (rel. June 24, 1985), *further recon. granted in part, Memorandum Opinion and Order,* MM Docket No. 83-46, FCC 86-410, 1 FCC Rcd 802 (1986).

10 *Id.* at 1033 n.85.

11 *See* 47 C.F.R. § 73.3555 n.2 (an "insulated" limited partner is one certified as having "no material involvement, directly or indirectly, in the management or operation of the media activities of the partnership").

12 *See Second Report and Order, Implementation of Sections 11 & 13 of Cable Television Consumer Protection and Competition Act of 1992 -- Horizontal and Vertical Ownership Limits,* MM Docket No. 92-264, 8 FCC Rcd 8565, 8568-69, 8577-8579 (1993) ("*Horizontal/Vertical Ownership Order*"). In the *Horizontal/Vertical Ownership Order,* the Commission voluntarily stayed the effective date of the horizontal ownership rules pending final judicial resolution of the District Court decision in *Daniels Cablevision, Inc. v.*

ensure competition and diversity in the video marketplace. In adopting the broadcast attribution standard for our rules restricting horizontal and vertical ownership, we also were guided by the legislative history of the 1992 Cable Act, which expressly suggested use of the broadcast attribution standard, and which directed that, along with the dangers of increased concentration, we should also consider the potential benefits of increased concentration -- e.g., increased economies of scale and increased capital investment in cable programming.[14] In light of these considerations, we found that a more restrictive attribution standard than the broadcast standard was not warranted for application to the structural rules.

5. We have adopted a more restrictive attribution standard, however, for those rules designed not only to promote competition and diversity, but also to deter specific discriminatory or improper conduct by cable operators or programmers. In contrast to the broadcast attribution standard, this more restrictive standard (1) considers a cable operator to have an attributable interest if it holds 5% or more of an entity's stock, whether voting or non-voting, (2) does not apply the single majority shareholder rule, and (3) attributes limited partnership interests of 5% or more, regardless of insulation.

6. We have adopted the more restrictive standard for our

United States, 835 F. Supp. 1, 10 (D.D.C. 1993), *aff'd in part, Time Warner Entertainment Co., L.P. v. FCC*, 93 F.3d 957 (D.C. Cir. 1996), which held that the underlying statute violates the First Amendment. *Horizontal/Vertical Ownership Order* at ¶ 3. In August 1996, the D.C. Circuit Court consolidated the *Daniels* appeal and *Time Warner Entertainment Co., L.P. v. FCC*, No. 94-1035 (D.C. Cir. 1994), a challenge to the Commission's rules. *Time Warner Entertainment Co., L. P. v. FCC*, 93 F.3d 957, 979-80 (D.C. Cir. 1996). The D.C. Circuit determined to hold court proceedings in abeyance while the Commission reconsidered the horizontal ownership rules. *Id.*

13 *Horizontal/Vertical Ownership Order*, 8 FCC Rcd at 8593-8596.

14 *See Report of the Senate Committee on Commerce, Science and Transportation*, S. Rep. No. 92, 102d Cong., 1st Sess. 80 (1991). Congress' intent is reflected in the 1992 Cable Act § 11(f)(2), 47 U.S.C. § 533(f)(2), which requires the Commission to weigh both the dangers and the benefits of increased concentration in promulgating our rules.

rules imposing specific behavioral restraints on cable operators and programmers, such as our rules regarding program access and program carriage, both of which were designed, in part, to prevent cable operators from using their market power to engage in improper conduct.[15] In our program access rulemaking, we noted that the more restrictive standard was being adopted in light of Congress' purpose in adopting Section 628: curbing certain incentives to influence the behavior of affiliates to the detriment of competitors.[16] While we acknowledged that one of the rule's objectives was to promote general competition and diversity in the video marketplace, the additional anti-discrimination objective warranted "a relatively inclusive attribution rule."[17] Similarly, in the MMDS and SMATV cross-ownership context, we adopted the more restrictive attribution standard in order to prevent cable operators from "warehousing potential competition," as well as to encourage the development of competition to established cable operators by alternative multichannel video service providers.[18]

7. In addition, we have relied upon our attribution rules in defining when an entity is considered an "affiliate" for certain purposes under Title VI. For instance, we have applied the more restrictive attribution standard to the ratemaking context, for purposes

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15 *See Program Access Order*, 8 FCC Rcd at 3370-71; *Program Carriage Order*, 9 FCC Rcd at 2650. *See also* 47 C.F.R. §§ 76.1000(b), 76.1300(a).

16 *See Program Access Order*, 8 FCC Rcd at 3370-71, *citing Second Report and Order, Recommendation to Congress, and Second Further Notice of Proposed Rulemaking, Telephone Company-Cable Television Cross-Ownership Rules, Section 63.54 - 63.58*, CC Docket No. 87-266, 7 FCC Rcd 5781 (1992); *see also Mem. Op. on Recon. of Program Access Order*, 10 FCC Rcd 1902, 1911-27 (rejecting various proposed exemptions from 5% attribution standard).

17 *Program Access Order*, 8 FCC Rcd at 3360, 3370. *See* 47 C.F.R. § 76.1000(b).

18 *See Report and Order and Further Notice of Proposed Rulemaking, Implementation of Sections 11 & 13 of Cable Television Consumer Protection and Competition Act of 1992 -- Cross-Ownership Limitations and Antitrafficking Provisions*, MM Docket No. 92-264, 8 FCC Rcd 6828, 6843-46 (1993); *see also* 47 C.F.R. §§ 21.912 n.1, 76.501(d)-(e).

of analyzing asset transfers and the provision of services between a cable operator and its affiliate.[19] We found that, in enacting the 1992 Cable Act, Congress intended to ensure that consumers pay reasonable rates for regulated cable services, and that it would be inconsistent with Congress' intent to allow cable operators to impose the costs of nonregulated activities on regulated cable services through improper cross-subsidization.[20] To deter such conduct, we held that the more restrictive attribution rule should apply. We also applied the more restrictive attribution standard to our rules limiting the amount of pass-throughs permitted for programming services affiliated with cable multiple system operators.[21] Those rules arose out of a concern about abuses that might occur if a vertically integrated cable operator were permitted to engage in unlimited pass-throughs to subscribers of the cost of programming that the operator obtained from an affiliated entity.[22]

8. Similarly, in adopting a definition of "affiliate" for purposes of the leased access provisions[23] and the open video system provisions,[24] we adopted the more restrictive attribution standard.[25]

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19 *See Report and Order and Further Notice of Proposed Rulemaking, Implementation of the Cable Television Consumer Protection and Competition Act of 1992 -- Rate Regulation and Adoption of a Uniform Accounting System for Provision of Regulated Cable Services,* MM Docket No. 93-215, 9 FCC Rcd 4527, 4663-68 (1994). *See also* 47 C.F.R. § 76.924(i).

20 *Id.* at 4663-64.

21 *See Report and Order and Further Notice of Proposed Rulemaking, Implementation of the Cable Television Consumer Protection and Competition Act of 1992 -- Rate Regulation,* MM Docket No. 92-266, 8 FCC Rcd 5631, 5787-88 (1993), *citing* 47 C.F.R. § 76.1000(b).

22 *Id.*

23 Communications Act § 612, 47 U.S.C. § 532.

24 Communications Act § 653, 47 U.S.C. § 573.

25 *See* 47 C.F.R. §§ 76.970(b), 76.1500(g); *Second Report and Order and Second Order on Reconsideration of the First Report and Order, Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992 -- Leased Commercial Access,*

We found that, in addition to promoting diversity, these provisions were designed to reduce the likelihood that cable operators and open video system operators will discriminate against or otherwise disfavor unaffiliated programming providers.[26] Given these dual objectives, we found that the more restrictive attribution standard was the appropriate standard for identifying the interests at issue.[27]

9. Finally, we note that in the "Cable Act Reform" proceeding[28] we are reviewing appropriate definitions of "affiliate" under other provisions of the 1996 Act, including the small operator provisions,[29] the new prong of the "effective competition" test,[30] and the cable-telco buy-out provisions.[31] Pending the adoption of final rules, we requested comments on the appropriate definition of "affiliate" for the cable-telco buyout provisions[32] and established interim rules for the small operator and "effective competition" provisions. For the small operator provisions, the interim rule adopted the definition of "affiliate" used for purposes of our small system cost-of-service rules.[33] Thus,

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CS Docket No. 96-60, FCC 97-27, 12 FCC Rcd 5267 (1997), at paras. 118-121 ("*Leased Access Order*"); *Third Report and Order and Second Order on Reconsideration, Implementation of Section 302 of the Telecommunications Act of 1995; Open Video Systems*, CS Docket No. 96-46, FCC 96-334, 11 FCC Rcd 20227 (1996), at paras. 4-16 ("*OVS Order*").

26 *OVS Order* at para. 14; *Leased Access Order* at para. 119.

27 *OVS Order* at paras. 14-15; *Leased Access Order* at para. 119.

28 *See Order and Notice of Proposed Rulemaking, Implementation of Cable Act Reform Provisions of the Telecommunications Act of 1996*, CS Docket No. 96-85, FCC 96-154, 11 FCC Rcd 5937 (1996) ("*Cable Act Reform NPRM*").

29 *See* Communications Act § 623(m)(2), 47 U.S.C. § 543(m)(2).

30 *See* Communications Act § 623(l)(1)(D), 47 U.S.C. § 543(l)(1)(D).

31 *See* Communications Act § 652, 47 U.S.C. § 572.

32 *Cable Act Reform NPRM* at ¶ 96.

33 *Cable Act Reform NPRM*, 11 FCC Rcd at 5947-48, *citing* 47 C.F.R. § 76.934(a). *See also Sixth Report and Order and Eleventh Order on Reconsideration, Implementation of*

an entity is deemed affiliated with a small cable operator if that entity has a 20% or greater equity interest in the operator (active or passive) or holds de jure or de facto control over the operator.[34] By contrast, in the "effective competition" context, the Commission found it reasonable to adopt an interim rule that reflected the new Title I affiliation threshold that Congress has prescribed for other provisions of the Communications Act.[35] Under the new standard, an affiliate is an entity that (directly or indirectly) owns or controls, is owned or controlled by, or is under common ownership or control with, another person, where the term "own" means to have an equity interest (or the equivalent thereof) of more than 10%.[36]

10. *Notice.* As noted above, we released the *Broadcast Attribution Notice* and the *Broadcast Attribution Further Notice* to review our broadcast attribution standard. Among the issues on which we solicited comment in the *Broadcast Attribution Notice* were: (1) whether to increase the voting stock ownership benchmark from 5 percent to 10 percent;[37] (2) whether to increase the passive investor stock ownership benchmark from 10 percent to 20 percent;[38] (3) whether to restrict or eliminate our single majority shareholder exemption and whether to attribute nonvoting shares in certain circumstances, such as where the minority or nonvoting shareholder has contributed a significant

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Section of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket Nos. 92-266 & 93-215, FCC 95-196, 10 FCC Rcd 7393 (1995).

34 *See Cable Act Reform NPRM,* 11 FCC Rcd at 5947-48.

35 *Id.* at 5943-44.

36 *See* Communications Act § 3(1), 47 U.S.C. § 153(1); *see also* 47 C.F.R. § 76.1401(b).

37 *Broadcast Attribution Notice* at paras. 18-46.

38 *Id.* at paras. 47-50. We also invited comment on our tentative conclusion not to expand the passive investor class to include pension funds, investment and commercial banks, and certain investment advisors.

portion of the equity or debt financing;[39] (4) whether to revise our insulation criteria for limited partnership interests, and whether to adopt an equity benchmark for noninsulated limited partners;[40] (5) whether to treat interests in limited liability companies ("LLCs") and similar new business forms, such as registered limited liability partnerships ("RLLPs"), as we now treat limited partnerships;[41] (6) whether to eliminate the remaining aspects of our cross-interest policy that prevent individuals from having "meaningful" interests -- including key employee relationships, joint ventures, and nonattributable equity interests -- in two broadcast stations, or a daily newspaper and a broadcast station, or a television station and a cable system, when both outlets serve "substantially the same area;"[42] and (7) how to treat non-equity financial relationships and multiple business relationships that, although not individually attributable, could combine to create sufficient influence to warrant attribution.[43]

11. In addition to the issues raised in the *Broadcast Attribution Notice*, the *Broadcast Attribution Further Notice* explored additional proposals to increase the precision of the attribution rules. First, we invited comment on whether we should add a new "equity or debt plus" ("EDP") attribution rule. Under such a rule, where an interest holder is a program supplier or same-market media entity, we will attribute its otherwise non-attributable equity and/or debt interests in a licensee or other media entity subject to the cross-ownership rules if those aggregated interests exceed a specified benchmark, proposed to be set at 33 percent.[44] Second, we tentatively concluded that we should

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39 *Id.* at paras. 51-54.

40 *Id.* at paras. 55-63.

41 *Id.* at paras. at 64-75.

42 *Id.* at paras. 76-92.

43 *Id.* at paras. 93-100.

44 *Broadcast Attribution Further Notice* at paras. 8-25.

treat television time brokerage agreements or local marketing agreements ("LMAs") the same as radio LMAs, and also count radio and television LMAs toward all applicable ownership limits.[45] Third, we invited comment as to whether we should attribute joint sales agreements ("JSAs") in certain circumstances.[46] Fourth, we invited comments on a Commission staff study of attributable ownership interests in broadcast television stations, appended to the *Broadcast Attribution Further Notice*, and on the implications of this study regarding the impact of the proposed attribution rule changes, particularly as to the voting stock benchmarks.[47] Fifth, we sought comments on whether a transition period or grandfathering of existing interests is appropriate. We tentatively concluded that any grandfathering should apply only to the current interest holder and that interests acquired on or after December 15, 1994, the date of adoption of the *Broadcast Attribution Notice*, should be subject to any final rules adopted.[48] Finally, we invited comments as to whether we should apply broadcast attribution criteria and add a new EDP attribution rule for purposes of the cable/Multipoint Distribution Service ("MDS") cross-ownership restrictions.[49]

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[45] *Id.* at paras. 26-31. For purposes of applying the radio LMA rules, the Commission's rules define time brokerage as "the sale by a licensee of discrete blocks of time to a 'broker' that supplies the programming to fill that time and sells the commercial spot announcements in it." 47 C.F.R. § 73.3555(a)(4)(iii). The *Broadcast Attribution Further Notice* refers to LMAs as "those time brokerage agreements involving a broker that is a licensee of one or more stations in the same market as the brokered station." *Id.* at para. 2 n. 4.

[46] *Id.* at paras. 32-35. JSAs are agreements between broadcasters for the joint sales of broadcast commercial time. *Id.* at para. 33.

[47] *Id.* at paras. 36-38 and Commission staff study attached thereto.

[48] *Id.* at paras. 39-42. We reiterated that the issue of grandfathering of television LMAs would be addressed separately in the television local ownership proceeding. *Id.* at para. 40.

[49] *Id.* at paras. 43-44.

12. This *Notice* initiates a similar review of attribution issues as they specifically relate to our cable rules.[50] We note that the ownership attribution rules are intended to identify those relationships that confer on their holders a degree of influence or control over key business decisions, including budget, personnel, programming, and technology practices of cable entities, such that the holders should be subject to the Commission's regulations. In addition, the attribution rules may be used to identify ownership or other relationships that could provide the entities involved with economic incentives to operate in conflict with the objectives of the particular cable regulation at issue. We seek comment on the same issues raised in the broadcast attribution proceedings as they pertain to the cable industry, and on whether and how these issues should factor into the review of our cable attribution rules. In particular, we ask commenters to focus on: (1) the proposed "equity or debt plus" addition to the current attribution rules, and specifically those relationships in the cable context that may provide sufficient incentive and ability for an otherwise nonattributable interest holder to exert an attributable influence or control; (2) the attribution of certain contractual or other business relationships in the cable context (including affiliations that allow different cable entities to purchase programming, technology or equipment on common terms, analogous to JSAs and LMAs in the broadcast context) that may implicate diversity and competition concerns, irrespective of debt or equity; (3) the impact of raising the stock ownership benchmark for active and passive investors in the cable context, particularly seeking empirical data and analysis similar to the Commission staff study on the same subject in the broadcasting context; (4) whether to retain, modify, or eliminate the single majority shareholder exemption; and

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[50] We have received informal communications suggesting such a comprehensive review of our attribution rules. *See, e.g.*, Letter from S. White Rhyne and Robert L. Petit of the Federal Communications Bar Association to Reed E. Hundt, dated January 30, 1995 (urging the Commission, as part of "reinventing government" efforts, to initiate a comprehensive review of the attribution tests used by its various bureaus and offices in order to promote consistency of interpretation and process).

(5) whether a transition period or grandfathering of existing interests is appropriate if we decide to adopt more restrictive attribution rules. Because the *Broadcast Attribution Notice* and the *Broadcast Attribution Further Notice* already address application of the attribution rules to the cable/MMDS and the cable/broadcast cross-ownership restrictions, we will not revisit and therefore do not seek comment on those issues in this proceeding.[51]

13. We seek comment on whether the assumptions underlying our cable attribution rules are still valid. In particular, we solicit comment on whether any relevant differences exist between the cable and broadcasting industries that would support a distinct cable attribution standard even for those cable rules designed, like our broadcasting ownership rules, to ensure competition and diversity. We note that the broadcast attribution rules focus primarily on those relationships which confer on their holders influence or control over a broadcaster's key business decisions in the areas of budget, personnel and programming. We seek comment on whether, in the cable context, these are the appropriate key business areas and whether the underlying areas of concern should include cable entities' technology decisions and practices. We seek comment on whether there are differences in ownership, financing or management structures, industry health, typical stockholdings, informal business arrangements, or outside financial claims that render one of the industries more or less subject to the types of influence or control that our attribution rules seek to identify. Also, because our current cable attribution rules do not distinguish between types of cable operators, we seek comment on whether any relevant differences exist among cable operators that would warrant different attribution rules.

14. We also solicit comment on whether and how we should re-evaluate the more restrictive attribution standard applicable to certain of the rules described above, such as the program access and program carriage rules and the cable/MMDS and cable/SMATV cross-ownership restrictions. In particular, we seek comment on: (1) wheth-

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[51] *See, e.g., Broadcast Attribution Further Notice* at paras. 3, 43.

er the more restrictive standard serves the purposes for which it was intended; (2) whether the more restrictive standard is over- or under-inclusive; (3) whether the more restrictive attribution standard should be revised in relation to the broadcast attribution standard; (4) whether these two attribution standards should be treated as completely separate and independent formulations; and (5) whether, in view of the purposes it serves, we should require a more compelling showing b efore modifying the more restrictive standard.

15. We seek comment on whether and how any changes in our cable attribution rules should affect our various definitions of "affiliate."[52] In particular, we seek comment on whether and how those affiliation rules that are expressly based on our cable attribution rules should change if the underlying attribution rules are changed.

16. We seek comment as to the business arrangements involved in recent cable system partnerships, joint ventures, swaps, transfers, mergers and acquisitions, particularly those transactions announced or consummated in 1997 or thereafter, including those discussed in the Commission's 1997 annual report on the status of competition in the delivery of video programming.[53] Commenters should identify the entities involved in each transaction, the projected date of consummation, details of the new structure including: the percentage and nature (e.g., voting or non-voting, limited or general partnership, insulated or non-insulated, rights of conversion) of each entity's ownership interests, the number of officers, directors, and other key personnel appointed by each entity to a management committee, board or other governing body, the portion of the equity or debt financing contributed by each entity, and any authority or power held by each entity to review, veto or otherwise influence the management or operation of the cable systems, as well as the ability to purchase

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[52] *See, e.g.*, 47 C.F.R. §§ 76.924(i), 76.970(b), 76.1500(g), 76.1401(b).

[53] *Fourth Annual Report, In the Matter of Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming*, FCC 97-423, CS Docket No. 97-141 at ¶¶ 142-148 (rel. Jan. 13, 1998).

programming, technology, or equipment under common contract terms. We seek information, in particular, as to any business arrangements undertaken to insulate one or more parties to these transactions from control or influence over key business aspects of the cable systems at issue. We also seek comment as to the development of the Commission's cable attribution rules to avoid inconsistency with any other statutes or regulations (e.g., those of the Internal Revenue Service or the Financial Accounting Standards Board) that may influence the structuring of the business arrangements at issue.

17. With respect to each ownership or relational interest discussed herein, we seek comment on whether the specified level or degree of ownership interest in, or relationship to, an entity would be likely to impart the ability to influence or control the operations of that entity, including core areas such as budget, personnel, programming, technology, or competitive practices, such that the ownership rules should be implicated. Consistent with the purpose of Section 257 of the 1996 Act to reduce market entry barriers for small businesses,[54] we also seek comment on the impact that any changes to our cable ownership attribution or affiliation standards will have on market entry barriers for small businesses. We ask interested parties to support their comments with empirical data and economic analyses regarding levels of influence in business organizations and current market conditions.

III. CONCLUSION

18. The cable attribution rules play a crucial role in the Commission's effort to ensure a competitive, diverse, and fair video marketplace. The purpose of this review is to examine whether our current cable attribution rules are accomplishing those goals, and to determine whether fewer, additional or different restrictions are warranted.

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[54] *See* 47 U.S.C. § 257.

VII. ORDERING CLAUSES

36. Accordingly, IT IS HEREBY ORDERED that pursuant to the authority in Sections 4, 303, 612, 613, 616, 623, 628, and 653 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154, 303, 532, 533, 536, 543, 548, 572 and 573, NOTICE IS HEREBY GIVEN of proposed amendments to Part 76, in accordance with the proposals, discussions, and statement of issues in this *Notice of Proposed Rulemaking*, and that COMMENT IS SOUGHT regarding such proposals, discussion, and statement of issues.

37.IT IS FURTHER ORDERED that the Commission's Office of Public Affairs, Reference Operations Division, shall send a copy of this *Notice of Proposed Rulemaking*, including the Initial Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration in accordance with paragraph 603(a) of the Regulatory Flexibility Act, Pub. L. No. 96-354, 94 Stat. 1164, 5 U.S.C. §§ 601 *et seq.* (1981).

FEDERAL COMMUNICATIONS COMMISSION

Magalie Roman Salas
Secretary

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of Section 11(c)	)	
of the Cable Television Consumer Protection		
and Competition Act of 1992 92-264	)	MM Docket No. 92-264
	)	
Horizontal Ownership Limits	)	

MEMORANDUM OPINION AND ORDER ON RECONSIDERA TION AND FURTHER NOTICE OF PROPOSED RULEMAKING

Adopted: June 23, 1998 Released: June 26, 1998
Comment date: August 14, 1998
Reply comment date: September 3, 1998

By the Commission: Commissioner Furchtgott-Roth issuing a separate statement; Commissioner Tristani dissenting in part and issuing a separate statement.

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Appendix A: List of Commenters

I. INTRODUCTION

1. This *Second Memorandum Opinion and Order on Reconsideration and Further Notice of Proposed Rulemaking* ("*Second Order on Reconsideration*" or "*Further Notice*") addresses petitions for reconsideration of the *Second Report and Order* in MM Docket No. 92-264[1] ("*Second Report and Order*") filed by the Center for Media Education/Consumer Federation of America ("CME/CFA") and Bell Atlantic Corporation ("Bell Atlantic").[2] Among other things, the *Second Report and Order*

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[1]8 FCC Rcd 8565 (1993).

[2]Petition for Reconsideration of Center for Media Education & Consumer Federation of America (filed Dec. 15, 1993); Petition of Bell Atlantic for Limited Reconsideration (filed Dec. 15, 1993).

promulgated rules pursuant to Section 613 of the Communications Act, which requires the Commission to "prescribe rules and regulations establishing reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such a person, or in which such a person has an attributable interest" ("horizontal ownership rules").[3] The Commission's horizontal ownership rules established in the *Second Report and Order* provide that "no person or entity shall be permitted to reach more than 30% of all homes passed nationwide through cable systems owned by such person or entity or in which such person or entity holds an attributable interest."[4] In addition, ownership of cable systems that reach up to 35% of all homes passed nationwide is permitted "provided the additional cable systems, beyond 30% of homes passed nationwide, are minority-controlled."[5]

2. In the *Second Report and Order*,[6] the Commission voluntarily stayed the effective date of the horizontal ownership rules pending final judicial resolution of the District Court decision in *Daniels Cablevision, Inc. v. United States*,[7] which held that the underlying statute violates the First Amendment. The *Daniels* court expressly recognized that "there is substantial ground for difference of opinion" as to the constitutionality of the underlying statute, meriting an

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[3]Section 613 was adopted as Section 11(c) of Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460, 47 U.S.C. § 533(f)(1)(A).

[4]47 C.F.R. § 76.503. As specified under 47 C.F.R. § 76.503, note 1 (c), "Attributable Interest" is defined by reference to the criteria set forth in the Notes to the Commission's cable cross-ownership rules, 47 C.F.R. § 76.501.

[5]47 C.F.R. § 76.503(b). For purposes of this regulation, "minority-controlled" is defined as "more than 50% owned by one or more members of a minority group." 46 C.F.R. § 76.503, note 1(a).

[6]*Second Report and Order* at ¶ 3.

[7]*Daniels Cablevision, Inc. v. United States*, 835 F. Supp. 1, 10 (D.D.C. 1993), *aff'd in part, rev'd in part, Time Warner Entertainment Co., L.P. v. FCC*, 93 F.3d 957 (D.C. Cir. 1996).

immediate appeal of its judgment.[8] Accordingly, rather than enjoining the Commission from adopting and enforcing horizontal ownership rules, the court stayed further court proceedings, including determination and imposition of relief for the plaintiffs, pending appeal.[9] On December 15, 1993, CME/CFA moved that the Commission lift its administrative stay.[10] The following month, Time Warner challenged the stayed rules in the D.C. Circuit Court in *Time Warner Entertainment Co., L. P. v. FCC.*[11] In August 1996, the D.C. Circuit Court consolidated the *Daniels* appeal regarding the facial validity of the statute and the *Time Warner* challenge to the Commission's rules, and determined to hold court proceedings in abeyance while the Commission reconsidered the horizontal ownership rules.[12]

3. In this *Second Order on Reconsideration*, the Commission maintains the current 30% horizontal ownership limit and denies the motion to lift the voluntary stay on enforcement of that limit. We note that, while the most established programmers can obtain favorable terms from even the large cable multiple system operators ("MSOs"), the cable horizontal ownership rules remain necessary to prevent MSOs from exercising market power against new, independent, and less prominent programmers.[13] In order to facilitate monitoring of cable ownership interests, the Commission hereby lifts the voluntary stay insofar as it applies to the information reporting requirements of 47 C.F.R. § 76.503(c). Prior to acquiring attributable interests in any

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[8] *Id.* at 12.

[9] *Id.*

[10] CME/CFA Motion to Lift Stay (filed Dec. 15, 1993).

[11] *Time Warner Entertainment Co., L. P. v. FCC*, No. 94-1035 (D.C. Cir. 1994).

[12] *Time Warner Entertainment Co., L.P. v. FCC*, 93 F.3d 957, 979-80 (D.C. Cir. 1996).

[13] The consequent growth of these alternative programmers ultimately may help to check the exercise of market power by the most established programmers.

additional cable systems, a person holding an attributable interest in cable systems reaching 20% or more of homes passed nationwide will be required to notify the Commission of the incremental change the acquisition makes in terms of the 30% of homes passed standard, i.e. specifying the ownership in terms of homes passed before and after the acquisition is complete.

4. In the *Further Notice*, we seek comment on possible revisions of the horizontal ownership rules and the method by which horizontal ownership is calculated. Specifically, we ask whether changes are needed to provide a more accurate measure of horizontal concentration to reflect changes in the market as alternative MVPDs continue to grow in the future. The *Further Notice* seeks comment on two possible changes in the manner that the rules are applied: (1) whether the rules should consider the presence in the market of all MVPDs rather than cable operators alone; and (2) whether the rules should be based on actual subscribers rather than on homes passed. Specifically, comment is sought on whether the rules should provide that the number of cable subscribers an entity is authorized to reach through cable systems, when combined with the number of subscribers reached by that entity through other MVPD systems, may not exceed 30% of all MVPD subscribers nationwide.

II. BACKGROUND

5. The 1992 Cable Act and its legislative history indicate heightened Congressional concern regarding horizontal concentration among cable multiple system operators. Witnesses at the Congressional hearings, including representatives of the MSOs themselves, testified to the need for cable horizontal ownership limits to preserve competition and protect the public interest.[14] Section 613(f) of the Communications Act (Section 11(c) of the 1992 Cable Act) requires that the Commission, "[i]n order to enhance effective competition . . .

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[14]*See, e.g., Report of the Senate Committee on Commerce, Science and Transportation*, S. Rep. No. 92, 102d Cong., 1st Sess. 34 (1991) ("Senate Report") (testimony of John Malone, TCI Chairman, regarding need for cable horizontal ownership limits).

prescribe rules and regulations establishing reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such a person, or in which such a person has an attributable interest."[15]

6. In adopting Section 613, Congress also recognized that multiple system ownership can benefit consumers. The House Report stated that cable industry consolidation has benefited consumers by allowing efficiencies in the administration, distribution and procurement of programming, and also noted that concentration of cable MSOs may help promote the introduction of new programming services by providing capital and a ready subscriber base for new services.[16] The House Report also observed that large cable MSOs can take competitive and programming risks that smaller operators cannot.[17] Similarly, the Senate Report acknowledged that horizontal concentration can create efficiencies from lower transaction costs in carriage negotiations between programmers and cable operators.[18]

7. Recognizing these conflicting factors, Congress directed in Section 613(f)(2) that, in addition to other public interest concerns, the Commission must consider and balance seven particular public interest objectives:

(1) to ensure that no cable operator or group of cable operators can unfairly impede the flow of video programming from the programmer to the consumer;

(2) to ensure that cable operators do not favor affiliated video programmers in determining carriage and do not unreasonably restrict the flow of video programming

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[15]47 U.S.C. § 533(f)(1)(A).

[16]*Report of the House Committee on Energy and Commerce*, H.R. Rep. No. 102-628, 102d Cong., 2d Sess. 43 (1992) ("House Report").

[17]*Id.*

[18]Senate Report at 33.

of affiliated video programmers to other video distributors;

(3) to take account of the market structure, ownership patterns, and other relationships of the cable industry, including the market power of the local franchise, joint ownership of cable systems and video programmers, and the various types of non-equity controlling interests;

(4) to take into account any efficiencies and other benefits that might be gained through increased ownership or control;

(5) to make rules and regulations that reflect the dynamic nature of the communications marketplace;

(6) to impose no limitations that prevent cable operators from serving previously unserved rural areas;

(7) to impose no limitations that will impair the development of diverse and high quality programming.[19]

8. Based on an assessment of these factors, in the *Second Report and Order*, the Commission adopted a horizontal ownership

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[19]47 U.S.C. § 533(f)(2). Beginning in 1994, the Commission has issued annual reports on the status of competition in the delivery of video programming. In these annual *Competition Reports*, the Commission has noted the potential benefits as well as the potential competitive concerns of increased national horizontal concentration among cable MSOs. *See First Annual Report, In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, FCC 94-235, CS Docket No. 94-48, 9 FCC Rcd 7442 at ¶¶ 148-155 (1994) ("*1994 Competition Report*"); *Second Annual Report, In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, FCC 95-491, CS Docket No. 95-61, 11 FCC Rcd 2060 at ¶¶ 131, 146 (1995) ("*1995 Competition Report*"); *Third Annual Report, In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, FCC 96-496, CS Docket No. 96-133, 12 FCC Rcd 4358 at ¶¶ 138-139 (1997) ("*1996 Competition Report*"); *Fourth Annual Report, In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, FCC 97-423, CS Docket No. 97-141 at ¶¶ 140-14, 149 (rel. Jan. 13, 1998) ("*1997 Competition Report*").

limit prohibiting any person from having an attributable interest in cable systems that in the aggregate reach more than 30% of cable homes passed nationwide. We found that this 30% ownership limit struck the proper balance between (1) ensuring that the structure of the cable industry nationwide limited the possibility that large cable MSOs might exercise excessive market power in the purchase of video programming, and (2) ensuring that the majority of MSOs could continue to expand and benefit from the economies of scale necessary to encourage investment in new video programming services, diverse program offerings, and the deployment of advanced cable technologies.[20] In order to promote minority ownership and diversity, we also adopted the minority-control allowance, which allows an MSO to reach an additional 5% of homes passed by cable nationwide if these homes are reached by cable systems that are more than 50% owned by one or more members of a minority group.[21]

III. ISSUES ON RECONSIDERATION

A. Requests to Lower the Current 30% Ownership Limit

9. In its reconsideration petition, CME/CFA requested that the Commission lower the current limit on the number of homes passed by cable systems owned by any one entity from 30% to 10%-20%.[22] Viacom, in its comments, argued for a 15% limit.[23] The arguments raised by CME/CFA and Viacom against the Commission's 30% limit fall into five broad categories -- consideration of diversity issues; alteration of the status quo; divestiture by Tele-Communications, Inc. ("TCI"); current levels of horizontal concentration; and impact of other statutes and rules. We address the arguments for each category below.

1. Consideration of Diversity Issues

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[20] *Second Report and Order* at ¶ 25.

[21] *Id.* at ¶ 28.

[22] CME/CFA Petition at 4.

[23] Viacom Comments on CME/CFA Petition at 2.

a. Background

10. CME/CFA argued that the Commission did not give sufficient consideration to media diversity concerns in setting the 30% limit and that "[p]romoting First Amendment diversity may well require limits below that needed to address anticompetitive concerns alone."[24]

11. Opposing reconsideration of the 30% limit, TCI noted that the CME/CFA diversity argument does not even attempt to balance the pros and cons of horizontal concentration, as the Commission is required to do by Section 613. TCI noted that Congress, the Commission, the courts, and antitrust scholars and economists uniformly have recognized that horizontal ownership can enhance consumer welfare and that this enhancement must be considered in addition to diversity aims. CME/CFA's diversity argument focuses only on the potential negative consequences of horizontal concentration.[25]

b. Discussion

12. Congress specifically directed that the Commission "impose no limitations that will impair the development of diverse and high quality programming."[26] Promoting diversity of ownership has

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[24]CME/CFA Petition at 3-4.

[25]TCI Opposition to CME/CFA Petition at 2-3.

[26]47 U.S.C. § 533(f)(2)(G); *see also* House Report at 42-43 ("[D]iversity of information sources can only be assured by imposing limits on the ownership of media outlets that are substantially below those that a traditional antitrust analysis would support"); Senate Report at 32 ("[T]here are special concerns about concentration of the media in the hands of a few who may control the dissemination of information. The concern is that the media gatekeepers will (1) slant information according to their own biases, or (2) provide no outlet for unorthodox or unpopular speech because it does not sell well, or both.").

been a long-standing policy of the Commission.[27] Diversity of information sources and viewpoints can be threatened by substantial concentration among cable system operators. Moreover, as the Commission has found, entry by new MVPDs is neither cheap nor easy and cable system operators remain the dominant distributors of video programming.[28] As a result, decreases in diversity of information sources or viewpoints that accompany increased concentration among purchasers of programming may not be easily remedied.

13. Diversity is not the sole factor the Commission must consider in promulgating the cable horizontal ownership limits. As indicated above (paragraph 7), Section 613 lists seven public interest factors that the Commission must balance in making a decision.[29] Before reaching a determination that 30% was a proper limit, the Commission twice requested public comment regarding the benefits and problems of horizontal concentration among cable MSOs.[30] In addition to considering diversity aims, the Commission considered the possibility that large MSOs might have the ability to preclude the launch of new video programming services (as required by public interest factors (1) and (2) above), the benefits and efficiencies that result from horizontal concentration (as required by public interest

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[27]For a broad assessment of the Commission's diversity analysis in the mass media context, *see Further Notice of Proposed Rule Making, Review of the Commission's Regulations Governing Television Broadcasting*, MM Docket No. 91-221, 10 FCC Rcd 3524 at ¶¶ 54-80 (1994).

[28]*1997 Competition Report* ¶¶ 126, 128, 150.

[29]*See* 47 U.S.C. § 533(f)(2).

[30]*See Notice of Proposed Rule Making and Notice of Inquiry, Implementation of Sections 11 and 13 of the Cable Television Consumer Protection and Competition Act of 1992*, 8 FCC Rcd 210 at ¶ 37 (1992) ("*First Notice and NOI*"); *Report and Order and Further Notice of Proposed Rule Making, Implementation of Sections 11 and 13 of the Cable Television Consumer Protection and Competition Act of 1992*, 8 FCC Rcd 6928 at ¶¶ 139-52 (1993) ("*First Report and Further Notice*").

factor (4)), and the relative impact of other statutes and rules in addressing competitive concerns regarding large MSOs.[31] In the *Second Report and Order*, the Commission specifically noted that Section 19 of the 1992 Cable Act (the program access requirements), Sections 4 and 5 of the 1992 Cable Act (the must-carry requirements), and Section 612 of the Communications Act (the leased access requirements), combined with the 30% ownership limit, "will be appropriate to address the diversity aims which underlie the statutory horizontal ownership provisions."[32] The Commission also considered diversity in allowing ownership of additional cable systems up to 35% of cable homes passed, provided the additional cable systems are minority-controlled.[33]

14. We believe the 30% horizontal ownership limit adopted by the Commission provides considerable protection for diversity concerns. The record in this docket clearly demonstrates that the Commission took into consideration diversity concerns in adopting the 30% cable horizontal ownership limits. The Commission balanced those considerations, as required by Section 613, with many other factors, some of which support the growth of cable MSOs. In fact, the Commission's consideration of diversity concerns is reflected by the fact that we adopted a horizontal ownership limit lower than one that might have been indicated by a traditional antitrust analysis alone.[34] The Commission was concerned that a lower horizontal ownership limit could "impair the development of diverse and high quality

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[31] *Second Report and Order* at ¶¶ 25-26.

[32] *Id.* at ¶ 26.

[33] *Id.* at ¶ 28.

[34] House Report at 42-43. In monopolization cases, the burden is on the plaintiff to prove that the defendant has monopoly power and this "virtually never" occurs when a defendant has a market share less than 50%. ABA Section of Antitrust Law, *Antitrust Law Developments (Fourth)* 236 (1997).

programming."[35] The Commission properly concluded that a 30% limit is generally appropriate to prevent the largest MSOs from gaining excessive leverage, and also ensures that the majority of MSOs continue to expand and obtain the economies of scale necessary to encourage investment in new video programming services and the deployment of advanced cable technologies.[36]

2. Alteration of the Status Quo

a. Background

15. CME/CFA asserted that the 30% horizontal ownership limit is too high because it does not alter the status quo. CME/CFA contended that the Commission "failed to acknowledge that existing levels of horizontal concentration are too high," citing a passage from the Senate Report stating that large MSOs have market power vis-a-vis programmers.[37] Arguing that Congress had made a specific finding that MSOs have the power to exact equity from programmers in exchange for carriage, CME/CFA asserted that Congress sought to change the status quo in the 1992 Cable Act.[38] In their reply comments, CME/CFA argued, without citing any specific legislative history, that the 1992 Cable Act was intended to reverse the Commission's decision in the *1990 Cable Report* not to adopt ownership limits.[39] CME/CFA stated that the 30% limit in the *Second Report and Order* resembles the balance struck by the Commission in its *1990 Cable Report* more than those envisioned in the 1992 Act, and that the *Second Report and Order* substituted the *1990 Cable Report* judgment for the requirements of the

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[35]47 U.S.C. § 533(f)(2)(G).

[36]*Second Report and Order* at ¶ 25.

[37]CME/CFA Petition at 4 (citing Senate Report at 24, 33).

[38]*Id.* at 4-11.

[39]CME/CFA Reply to Oppositions at 2-4 (citing *Rate Deregulation & the Commission's Policies Relating to the Provision of Cable Television Serv., Report on Competition*, 5 FCC Rcd 4962 (1990) ("*1990 Cable Report*")).

1992 Cable Act.[40]

16. Time Warner Entertainment Co., L.P. ("Time Warner") and the National Cable Television Association ("NCTA") argued the Commission was given the discretion to balance competing concerns by Congress and disagreed that the 1992 Cable Act requires the Commission to alter the status quo.[41]

b. Discussion

17. The issue here is one of statutory interpretation -- whether Congress, in enacting Section 613, made a final determination that then current levels of horizontal concentration were too high, requiring the Commission to adopt rules to force divestiture and to reduce horizontal concentration. We believe that the text of Section 613 is clear that the Commission was given the discretion to adopt limits that may or may not require divestiture.

18. Section 613 gives the Commission the discretion "to prescribe rules and regulations establishing *reasonable limits* on the number of cable subscribers a person is authorized to reach ...."[42] CME/CFA's argument ignores that the statute does not direct the Commission to alter the status quo by ordering divestiture by any cable MSO. Instead, Congress required that the Commission set "reasonable limits" and left the parameters of what "reasonable limits" would be to Commission discretion.

19. Further, we note that this construction of the statute is supported by the legislative history. The Senate Report explicitly states that "[t]he legislation does not imply that any existing company must be divested and gives the FCC flexibility to determine what limits are

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[40]*Id.* at 2-4.

[41]Time Warner Opposition to CME/CFA Petition at 7-8; NCTA Opposition to CME/CFA Petition at 7-8.

[42]47 U.S.C. § 533(f)(1)(A) (emphasis added).

reasonable."[43] The House Report states that: "Currently, the largest MSO controls access to almost 25 percent of all US cable subscribers. Although this percentage may appear low relative to other industries, the Committee believes that it may be quite significant depending on the subscriber level needed to launch and sustain a cable programming service."[44] The language of the House Report is significant on this point. While it demonstrates Congress' concern about current levels of horizontal concentration, it expressly does not make a final conclusion, but simply states that current levels "may be quite significant depending on" the number of subscribers needed to launch and sustain a programming service.[45]

20. The statute and the legislative history make clear that the Commission was not required to alter current industry structure, but to consider the potential public interest concerns associated with the industry structure. The Commission fully considered such interests.

3. Divestiture by TCI

a. Background

21. CME/CFA asserted that the *Second Report and Order* was too concerned about avoiding divestiture by TCI and was not focused on consumer welfare.[46] Arguing that the legislative history of Section 613 indicates that divestiture might be warranted, CME/CFA contended that a passage in the Senate Report stating that the legislation "does not imply that any existing company must be divested" expressly left open the possibility of divestiture.[47] CME/CFA urged that the Commission not be deterred from imposing horizontal limits which

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[43]Senate Report at 34.

[44]House Report at 42.

[45]*Id.*

[46]CME/CFA Petition at 4-11.

[47]*Id.* (quoting Senate Report at 34).

would require TCI to divest, as Congress required the Commission to weigh seven public interest considerations, none of which was to ensure that MSOs could continue to expand.[48]

22. Viacom agreed with CME/CFA that the *Second Report and Order* placed too much reliance on language in the Senate Report which states that the limit "does not imply that any existing company must be divested." Viacom argued that the legislative history does not prohibit the Commission from adopting a limit that would require divestiture, but, at most, only indicates that the Commission should not promulgate rules which would impose divestiture if the divestiture were not in the public interest. Viacom stated that divestiture is relevant and should be considered by the Commission in adopting horizontal ownership rules, but that avoiding divestiture should not override the public interest concern regarding excess MSO market power against unaffiliated programmers.[49]

23. Time Warner, TCI, Liberty Media Corporation ("Liberty Media"), and NCTA responded that the Commission's decision not to order divestiture by TCI was based upon the finding that there was an "absence of definitive evidence that existing levels of ownership are sufficient to impede the entry of new video programmers or have an adverse effect on diversity."[50] Liberty Media argued that, since no programmer claimed in the original proceeding that any cable operator had exercised horizontal market power and no commenter introduced empirical evidence of such power, it was proper for the Commission to make this finding.[51] NCTA argued that avoiding divestiture was not the driving factor in the Commission's decision, as the Commission

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[48]CME/CFA Reply at 2-4.

[49]Viacom Comments at 7-8.

[50]Time Warner Opposition at 7-8; NCTA Opposition at 7-8; Liberty Media Reply at 9-11 (quoting *Second Report and Order* at ¶ 27).

[51]Liberty Media Reply at 9-11.

considered a number of factors in proposing and adopting the limits, including avoiding potential disruption in existing ownership and the absence of definitive evidence that existing levels of ownership are harmful.[52]

b. Discussion

24. We agree with Viacom and CME/CFA that the Commission has the authority under Section 613 to order divestiture. We disagree with CME/CFA to the extent they argue that the Commission should not consider the full impact divestiture would entail before promulgating such rules. Inquiry into the impact divestiture would have upon subscribers, programmers and industry investment are legitimate public interest objectives that the Commission is entitled to consider. A rule requiring divestiture must be based on consideration of all relevant factors.[53] We believe that the *Second Report and Order* properly considered whether the substantial structural change that divestiture would entail was warranted.

25. We reject CME/CFA's argument that the impact of ordering divestiture should not have entered into the Commission's decision-making because it is not one of the seven specifically-enumerated public interest factors of Section 613. The statute explicitly contemplates that the factors enumerated are "among other public interest objectives" that the Commission is to consider.[54] Assessing the impact

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[52]NCTA Opposition at 7-8 (quoting *Second Report and Order* at ¶ 27); NCTA Reply Comments at 3-4.

[53]In *Citizens to Preserve Overton Park, Inc. v. Volpe*, 401 U.S. 402 (1971), the Supreme Court held that courts reviewing agency action under the arbitrary and capricious standard must make a "searching and careful" examination of "whether the decision was based on a consideration of the relevant factors. . . ." *See also Greater Boston Television Corp. v. FCC*, 444 F.2d 841, 850-53 (D.C. Cir. 1970), *cert. denied*, 403 U.S. 923 (1971) (the function of a reviewing court "is to assure that the agency has given reasoned consideration to all the material facts and issues").

[54]47 U.S.C. § 533(f)(2); *see Greater Boston Television*, 444 F.2d at 850-53 ("Assuming consistency with law and the legislative mandate, the agency has latitude not merely

of divestiture is consistent with Section 613's directive that the Commission "take particular account of the market structure" and "not impose limitations which would impair the development of diverse and high quality video programming."[55]

26. In both the *First Report and Further Notice* and the *Second Report and Order*, the Commission considered arguments for low limits that would require divestiture. The Commission based its final decision not solely on a determination to avoid divestiture, as CME/CFA suggested, but, more importantly, upon the public interest requirements of Section 613. In its initial comments, the Association of Independent Television Stations, Inc. argued for a 10% subscriber cap.[56] In the *First Report and Further Notice*, the Commission stated that this proposal not only would require divestiture but "would sacrifice the efficiencies achieved by horizontal concentration."[57] The Commission determined that the proposal would "be contrary to the legislative history" of Section 613.[58] The Commission asked in the *First Report and Further Notice* that parties "favoring limits below 25%" that would require divestiture "discuss the effect that such divestiture would have on service to subscribers, programming carriage agreements, and on future MSO investment in new programming and technology."[59] The Commission emphasized the over-arching importance of striking "the proper balance among the competing public interest objectives Congress directed us to consider" in setting the horizontal ownership limit,

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to find facts and make judgments, but also to select the policies deemed in the public interest.").

[55]47 U.S.C. §§ 533(f)(2)(C), (E), (G).

[56]*See* Association of Independent Television Stations, Inc. Initial [Feb. 1993] Comments at 7; *First Report and Further Notice* at ¶ 146.

[57]*First Report and Further Notice* at ¶ 148.

[58]*Id.*

[59]*Id.* at ¶ 149.

without excluding the possibility of divestiture.[60]

27. In the *Second Report and Order*, the Commission again considered proposals that would have required divestiture by the largest MSO, TCI, and also discussed the other effects divestiture would create. The Commission, after considering the "statutory factors and . . . the preponderance of the data provided in the record," concluded that a 30% limit was appropriate because it would "prevent the nation's largest MSOs from gaining enhanced leverage from increased horizontal concentration" while "ensur[ing] that the majority of MSOs continue to expand and benefit" from the positive aspects of increased concentration.[61] The Commission expressly confronted the divestiture issue and explicitly determined that "in the absence of definitive evidence that existing levels of ownership are sufficient to impede the entry of new video programmers or have an adverse effect on diversity, existing arrangements should not be disrupted."[62]

4. Current Levels of Horizontal Concentration

a. Background

28. CME/CFA asserted that the *Second Report and Order* did not sufficiently address the evidence that the largest MSO, TCI, already has market power and uses its market power to disadvantage competing program services.[63] CME/CFA argued that, from a competitive standpoint, the Commission "fail[ed] to acknowledge that existing levels of horizontal concentration are too high."[64]

29. Viacom argued that a lower limit is needed because, based upon its own experience, 40 million subscribers are necessary for an advertising-supported, basic cable programming network to be

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[60] *Id.* at ¶ 134.

[61] *Second Report and Order* at ¶ 25.

[62] *Id.* at ¶ 27.

[63] CME/CFA Petition at 4-11.

[64] *Id.* at 2-4.

successful.[65] Viacom extrapolated from this figure its argument that no MSO should be allowed to come close to controlling access to enough subscribers that would prevent a programmer from reaching 40 million homes -- i.e., based on 1993 cable subscribership figures, no MSO should be allowed to come close to controlling access to 30.9% of cable subscribers. Viacom also asserted that the then current levels of market concentration allowed large MSOs to drive down the license fees they pay to programmers. This, Viacom argued, affects the entire market for license fees and drives them down across the board. The result is that programmers cannot spend as much on development, thus potentially reducing the diversity and quality of programming available to subscribers.[66]

30. Both CME/CFA and Viacom provided anecdotal evidence to support their belief that TCI, the nation's largest MSO, is too large. CME/CFA cited the Federal Trade Commission's ("FTC") agreement with TCI and Liberty Media forcing divestiture of QVC, Inc. ("QVC") as evidence that TCI possesses currently anticompetitive influence resulting from its large horizontal size.[67] In addition, CME/CFA cited Viacom's antitrust complaint against TCI and claimed that, according to the Viacom complaint, TCI had dropped Viacom's The Movie Channel in favor of TCI affiliate Encore Media, and had withheld affiliation with Viacom's Showtime to force Showtime either to merge with Encore Media or be destroyed.[68] CME/CFA asserted

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[65]Viacom Comments at 9. Viacom estimated that 40 million subscribers equaled approximately 69.1% of cable subscribers nationwide at the time of Viacom's filing. *Id.*

[66]*Id.*

[67]CME/CFA Petition at 7-8 (citing *TeleCommunications, Inc., et al.; Proposed Consent Agreement with Analysis to Aid Public Comment*, 58 Fed. Reg. 63167 (Nov. 30, 1993)).

[68]*Id.* at 8-9 (citing *Viacom International, Inc. v. Telecommunications, Inc., Liberty Media, et. al*, Civ. No. 93-CIV6658(KC) (filed S.D.N.Y. Sept. 23, 1993));

that, if TCI can wield power over Viacom and its popular networks, it certainly has power to preclude the launching of new programming from smaller programmers.[69] CME/CFA also cited a passage in the Senate Report stating that "[w]itnesses at the hearings testified that. . . [MSOs have the power] to determine what programming services can 'make it' on cable."[70] CME/CFA argued that independent programmers' failure to argue for lower levels of concentration previously in this docket indicates "their reasonable fear of offending the MSOs who, after all, have it in their power to put them out of business."[71]

31. Viacom stated that TCI's anticompetitive conduct led Viacom, after the initial comment periods in this proceeding closed, to file its antitrust complaint against TCI, Liberty Media and others and also convinced Viacom that stricter horizontal rules are necessary to prevent anticompetitive conduct in the market for programming services.[72]

32. All other cable operators filing comments strenuously opposed the argument that current levels of horizontal concentration are "too high." TCI stated that the arguments of CME/CFA and Viacom fail to recognize the current benefits of horizontal concentration, which the Commission is required to consider under its statutory mandate.[73] TCI also asserted that horizontal concentration allows

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CME/CFA Reply at 3.

[69]CME/CFA Petition at 7-11; CME/CFA Reply at 3.

[70]*Id.* (quoting Senate Report at 33).

[71]CME/CFA Petition at 3, 7-11.

[72]Viacom Motion for Leave to File Response and Response at 2-3. Pursuant to Section 1.415(d) of the Commission's rules, we deny Viacom's motion to submit its late-filed response. However, we will consider Viacom's response as informal comments under Section 1.419(b).

[73]TCI Opposition at 2-3.

MSOs to achieve economies of scale in research and development of transmission and distribution technology and achieve considerable savings in administrative costs such as billing operations, advertising, marketing, and management. In addition, Time Warner stated that the costs of negotiating with programmers are reduced on both sides of the table.[74]

33. TCI argued that under traditional antitrust analysis, the then current ownership level of MSOs did not equate to high concentration, citing legislative history which reported that the Herfindahl-Hirshman Index ("HHI") of the top 20 MSOs was 491 and the Four-Firm Ratio was 36%, well below the Department of Justice thresholds of 1,000 and 50%. TCI stated that these levels did not indicate that MSOs are able to extract unreasonable concessions from their suppliers.[75] Time Warner pointed out that an MSO's incentive to undertake a foreclosure strategy is counterbalanced by desires to increase subscribership and decrease churning of programming.[76] TCI also submitted a report from a group of economists that recommended against setting low ownership limits because, due to MSOs' recognition that their own success depends on the availability of a high quantity and quality of programming, increased concentration "will not affect the array of programming selected and distributed by the cable operator and therefore will not distort the allocation of resources in the production of program services."[77]

34. Cable MSOs and programmers also strongly disputed Viacom's suggestion that 40 million subscribers are required for suc-

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[74]Time Warner Opposition at 3-5; *see also* House Report at 43.

[75]*See* TCI Opposition at 4-5.

[76]Time Warner Opposition at 8-9; *see also* Senate Report at 24.

[77]Stanley M. Besen, Steven R. Brenner and John R. Woodbury, *An Economic Analysis of the FCC's Proposed Cable Ownership Restrictions* at 19-22 (attached to TCI Opposition).

cess. Several pointed out that a number of successful cable networks had never achieved penetration levels above 60% to 70%.[78] Time Warner argued that there is no "magic" level of penetration that necessarily assures, or prevents, a programming service's commercial success.[79] Turner Broadcasting System, Inc. ("TBS") pointed out in its opposition that ESPN2, an unaffiliated programmer, already had over 10 million subscribers, one million more than the vertically affiliated Cartoon Network, and the then-unaffiliated Sci-Fi Channel was regarded as successful with 15 million subscribers.[80] Liberty Media stated that 46 of the 68 listed national basic cable networks then had fewer than 40 million subscribers.[81]

35. TCI and Liberty Media responded to CME/CFA and Viacom's specific charges of anticompetitive conduct by arguing that the charges were unsupported. TCI argued that the consent decree cannot be used as evidence against TCI. TCI also stated that no competitive problems were ever proved in the QVC matter and that TCI divested its interest solely because it did not want to interfere with QVC's tender offer for Paramount.[82] Liberty Media argued that the agreement with the FTC was intended to address vertical concerns and

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[78]*See* Time Warner Opposition at 6-7 (BET and Country Music Television in operation for years with levels below 60-70%).

[79]Time Warner Reply to Viacom Comments at 6; Time Warner Opposition at 6-7.

[80]TBS Opposition to CME/CFA Petition at 2.

[81]Liberty Media Opposition at 10-11.

[82]*See* Testimony of John C. Malone (TCI Chairman and CEO) before the Senate Subcommittee on Antitrust, Monopolies and Business Rights (Dec. 16, 1993) (attached to TCI Opposition).

not horizontal size.[83] TCI and Liberty Media stated that Viacom's antitrust suit was filed in the context of its attempt to prevent QVC from acquiring Paramount. Given this history, TCI and Liberty Media argued that it would be improper for the Commission to decide its cable horizontal ownership limits based upon unproven allegations made by a competitor with the desire to enhance Viacom's efforts to increase its own ownership concentration in several markets.[84] TBS discounted Viacom's allegations against TCI as "an extension of its current jihad with TCI."[85] Time Warner stated that Viacom's argument consists of unproven allegations.[86]

36. Time Warner also pointed out that during the prior comment period, no programmer, either failed or successful, proposed or well-established, claimed that any cable operator exercised horizontal market power, and no commenter introduced any empirical evidence of the exercise of such market power.[87] Liberty Media argued that without this evidence, the Commission appropriately determined that cable horizontal ownership limits that freeze or reduce existing ownership levels were unjustified.[88]

b. Discussion

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[83] *See* Liberty Media Opposition at 9, quoting Statement of Mary Lou Steptoe before the Senate Subcommittee on Antitrust, Monopolies and Business Rights, Committee on the Judiciary 5-6 (Nov. 18, 1993) ("Since the alleged competitive problems stem from the vertical link between TCI/LMC and QVC, the FTC's consent order addresses them by severing that link.").

[84] TCI Opposition at 6-7; Liberty Media Opposition at 8-12; Liberty Media Reply at 12-15.

[85] TBS Response to Viacom's Comments at 1.

[86] Time Warner Reply at 3-5.

[87] *Id.* at 3-5.

[88] Liberty Media Opposition at 6.

37. As stated above, the Commission found in the *Second Report and Order* that 30% was an appropriate limit "in the absence of definitive evidence that existing levels of ownership are sufficient to impede the entry of new video programmers or have an adverse affect on diversity ..."[89] The legislative history of Section 613 indicates Congress' concern that excessive horizontal concentration had the potential to facilitate the anticompetitive exercise of monopsony power and adversely impact the diversity of programming.[90] Because cable MSOs generally purchase cable programming on a national level and at the same time distribute that programming to consumers on a local level through the locally franchised cable system, assessing the impact of cable concentration by examining both the national programming market and the local distribution market is appropriate. In the *Second Report and Order*, the Commission found that a 30% limit was "appropriate to prevent the nation's largest MSOs from gaining enhanced leverage from increased horizontal concentration."[91] The Commission then concluded that the 30% limit is "reasonable to prevent the types of anti-competitive conduct which concerned Congress, particularly when coupled with the behavioral restrictions contained in [the program access and program carriage provisions] .... "[92] In this reconsideration proceeding, no one has proffered any new evidence that requires the Commission to alter this finding. Moreover, we believe the 30% limit complies with the intent of Congress and satisfies the criteria specified in Section 613.

38. In enacting Section 613, Congress expressed concern about concentration of the media in the hands of a few "media gate-

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[89] *Second Report and Order* at ¶ 27.

[90] Senate Report at 32-33.

[91] *Second Report and Order* at ¶ 25.

[92] *Id.* at ¶ 26.

keepers" who could control dissemination of information.[93] The accumulation of market share on a national level by a single or small number of large cable MSOs could diminish the diversity of programming available to most households in the United States. As of June 1997, there were more than 64 million cable subscribers representing more than 66% of all television households in the United States.[94] As such, cable television remains a primary source of information and programming for many households in the United States. The 30% rule limits the extent to which one or a few large cable MSOs could reduce the diversity of programming in the United States.

39. The 30% limit diminishes the likelihood that either a large cable MSO acting unilaterally or a group of cable MSOs acting in concert could exercise market power in the purchase of programming.[95] While the exercise of market power could result in lower negotiated programming costs for these MSOs in the short run, it could also adversely affect the development of diverse and innovative programming in the long run. In addition to preserving the development of programming, the 30% limit decreases the likelihood that a large cable MSO acting unilaterally could coerce nonaffiliated programmers into denying programming to alternative MVPDs, such as a DBS provider.[96]

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[93]Senate Report at 32, 33.

[94]*1997 Competition Report* at ¶¶ 14 and 15.

[95]*See generally,* David Waterman and Andrew Weiss, VERTICAL INTEGRATION IN CABLE TELEVISION (1997) at 55-86 and 128-141.

[96]*See also* 47 U.S.C. § 548(b), which makes it "unlawful for a cable operator . . . to engage in unfair methods of competition or unfair or deceptive acts or practices, the purpose or effect of which is to hinder significantly or to prevent any multichannel video programming distributor from providing satellite cable programming or satellite broadcast programming to subscribers or consumers."

40. The 30% limit may serve to facilitate the development of competition in those markets where cable MSO market power already exists. The rule limits the extent to which large cable MSOs can merge and result in one or two MSO's controlling local cable markets nationwide. Limiting this merger potential may preserve opportunities for entry by overbuilders or other MVPD providers and reduce the likelihood that large MSOs can coordinate their behavior by mutually forbearing from overbuilding each other's service territories. Coordinated activity between cable MSOs, whether tacit or overt, is more likely with few firms than many (due to greater ease in reaching a consensus, monitoring compliance, and punishing cheaters), and such behavior will have a greater impact the larger combined share of the market these collusive firms control. The 30% limit also reduces the likelihood of coordinated activity between large cable MSOs in areas such as program purchasing and equipment purchasing (e.g., set top boxes and converters).[97]

41. The 30% limit permits cable MSOs to cluster systems in order to gain efficiencies related to economies of scale and scope in administration, deployment of new technologies and services, extension into previously unserved territories, etc..[98] Accordingly, the 30% limit simultaneously guards against the potential anticompetitive effects of horizontal concentration and allows cable MSOs to realize the benefits of clustering.

42. The 30% limit is a structural complement to the program

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[97] *See generally,* James L. Langenfeld and Louis Silvia, *Federal Trade Commission Horizontal Restraint Cases: An Economic Perspective,* ANTITRUST LAW JOURNAL (1993); Alexis Jacquemin and Margaret E. Slade, *Cartels, Collusion, and Horizontal Merger,* HANDBOOK OF INDUSTRIAL ORGANIZATION, Richard Schmalensee and Robert Willig, ed., (1990); *see also, NCAA v. University of Oklahoma,* 468 U.S. 85 (1984); *Northwest Wholesale Stationers, Inc. v. Pacific Stationary and Printing Co.,* 105 S.Ct. 2613 (1985).

[98] *E.g., Second Report and Order* at ¶¶ 25-26; *1997 Competition Report* at ¶¶ 140-148.

access provisions.[99] The horizontal ownership rules limit the potential for anticompetitive abuses of purchasing power in areas outside of the core areas covered by the program access rules, such as programming contracts between cable operators and non-vertically integrated programmers or contracts involving programming that is not delivered to cable operators via satellites. In addition, structural regulation generally is more easily enforced and detected than conduct regulation. We recognize that a large market share does not in and of itself indicate that a firm or a collection of firms has the ability to exercise market power or engage in anticompetitive behavior.[100] Nevertheless, structural regulation imposes far fewer economic costs on the market than regulatory models that use primarily price or case-specific conduct regulation as a way to mitigate strategic, anticompetitive behavior.[101]

43. It appears that the current level of concentration among cable MSOs has not prevented an expansion in programming sources and networks. The nation's largest cable MSO reached 24% of homes passed by cable in 1990;[102] grew to 27% by 1993;[103] and reached 29.32%

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[99]47 U.S.C. § 628; 47 C.F.R. § 76.1000 et seq.

[100]*See, e.g., In re Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier*, 11 FCC Rcd 3271 (1995). We also recognize that the courts have generally found that a firm can not successfully obtain a monopoly with less than a 30% market share. *Antitrust Law Developments (Fourth)* 298-99 and cases cited therein.

[101]*Cf., Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, *reh'g denied*, 509 U.S. 940 (1993).

[102]Senate Report at 32.

[103]*Second Report and Order* at n. 40.

at the time of the *1997 Competition Report*.[104] At the same time, our annual competition reports indicate a gradual but continuous growth and expansion in both cable-affiliated and independent programming sources and programming networks.[105] This evidence tends to suggest that the Commission properly struck a reasonable balance between concentration and diversity concerns. Thus, contrary to CFA's allegations, the actual evidence to date suggests that allowing a cable MSO to own systems reaching 30% of homes passed has not significantly hampered new video programmers' entry in the programming market.

44. Viacom's argument that 40 million subscribers are needed for a national cable programming network to be successful is not supported by the record. Other parties in the proceeding have presented evidence disputing Viacom's 40 million figure, including several examples of cable programming services (such as BET, Nickelodeon, ESPN2) that were successful before reaching 40 million subscribers. Prior comments in this docket also provide data that 40 million subscribers are not necessary for a national, basic cable programming network to be successful.[106] Commenters, including new networks, in other proceedings before the Commission likewise have

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[104] *1997 Competition Report* at Appendix E, Table E-3. Because the Commission's reporting requirements have been stayed along with the horizontal ownership limit, we currently do not have sufficient information regarding the many joint ventures and other transactions, recently announced by cable MSOs such as TCI, Cablevision, Adelphia, Falcon, Time-Warner, etc., to determine conclusively whether these transactions will result in attributable ownership interests that would place some MSOs above the 30% threshold.

[105] *Id.* at ¶ 158.

[106] *See* Time Warner Initial [Feb. 1993] Comments at 27-29 and TCI Initial [Feb. 1993] Comments at 24-25 (both listing several apparently successful national basic cable programming networks with below 40 million subscriber penetration).

stated that a new national, advertiser-supported network requires a threshold subscriber base of ten to twenty million subscribers.[107]

45. The *1997 Competition Report* estimates the total number of MVPD subscribers nationwide to be 73,646,970.[108] Consequently, a programmer that fails to sell its product to an MSO having 30% of cable homes passed nationwide still would have the opportunity to reach (through the remaining MVPDs) over 50 million subscribers, well over the threshold for national success. Many among the top 50 programmers nationwide, including MSNBC, the Disney Channel, and Turner Classic Movies, reach substantially less than 40 million subscribers.[109] Neither Viacom nor CME/CFA has provided sufficient grounds to warrant a lowering of the 30% horizontal ownership limit and freezing or reducing existing levels of cable ownership.

5. Impact of Other Statutory Provisions and Rules

a. Background

46. CME/CFA argued that the Commission's reliance in the *Second Report and Order* upon existing statutes and regulations, such as the program access and carriage rules, as a justification for higher ownership limits was improper because structural regulations provide

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[107] *See* Outdoor Life Network, Speedvision Network, The Golf Channel, BET on Jazz, and America's Health Network Comments at 11-13, 34, 36 in *Closed Captioning and Video Description of Video Programming, Implementation of Section 305 of the Telecommunications Act of 1996, Video Programming Accessibility*, MM Docket No. 95-176; Affidavit of Christopher H. Murvin at 8, Affidavit of Jefferi K. Lee at 6, and Affidavit of Roger Williams at 8 in *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation (Leased Access)*, MM Docket No. 92-266 & CS Docket No. 96-60; Program Providers Comments at 12 in *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation (Going Forward)*, MM Dockets Nos. 92-266 & 96-215.

[108] *1997 Competition Report* at Appendix E, Table E-1.

[109] *Id.* at Appendix F, Table F-6.

"a superior means of promoting diversity compared to behavioral regulations."[110]

47. Viacom also asserted that the Commission should not have relied on other sections of the 1992 Cable Act, such as program carriage and access provisions,[111] must-carry requirements,[112] channel occupancy limits,[113] and leased access requirements.[114] Viacom argued that Congress did not indicate that the Commission should calibrate the cable horizontal ownership rules to take these provisions into account, as these provisions were enacted with purposes separate from the cable horizontal ownership provision. Viacom stated that these other provisions probably will not have any practical impact on restraining anticompetitive conduct of cable operators: leased access is probably not a viable option for programmers, must-carry provisions are for television broadcasters (not unaffiliated programmers like Viacom), and the program access provisions only require MSOs to offer their own programming to other distributors. Viacom also argued that although the program carriage provisions prohibit cable operators from extracting a financial interest or exclusivity rights in exchange for programming carriage, the statute does not address the issue arising when an MSO "solely by virtue of the size of its subscriber base" has market power to determine whether a programming service can reach

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[110]CME/CFA Petition at 3. The Commission notes that in its original comments in this proceeding, CFA argued that the Commission should "proceed with great caution and consider the effect of implementation of the rate regulation and program access provisions of the 1992 Cable Act when creating rules with respect to cable ownership limits and concentration." CFA Initial [Feb. 1993] Comments at 3.

[111]47 U.S.C. §§ 536, 548.

[112]47 U.S.C. §§ 534, 535.

[113]47 U.S.C. § 533(f)(1)(B).

[114]47 U.S.C. § 532.

the critical mass of subscribers needed to succeed. Viacom also stated that programmers are not likely to bring program carriage complaints against the largest MSOs, who are their biggest customers and therefore essential to success.[115]

48. Liberty Media and Time Warner responded by arguing that the existing restrictions in the 1992 Cable Act support maintaining the 30% ownership limit. Liberty Media argued that the Commission properly considered the cumulative effect of these regulations to protect against the exertion of undue power over the success of new video services.[116] Time Warner agreed, stating that the cable horizontal ownership limits should not be viewed as an isolated measure and that the cumulative effect of all provisions and rules should be taken into account.[117] Liberty Media also pointed out that Viacom had taken completely the opposite position on this point in the initial comment round in this docket.[118] NCTA stated that Congress directed the Commission to take into account the market structure, ownership patterns and other relationships in the industry in establishing these limits, and that the Commission found that the cumulative effect of all these rules should protect against any one cable operator's exertion of excessive market power.[119]

b. Discussion

49. We believe that the *Second Report and Order* properly considered the impact of other rules and statutes since the public interest requirements of Section 613 require the Commission to examine the marketplace as it currently operates, which includes the effects

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[115]Viacom Comments at 4-5.

[116]Liberty Media Opposition to CME/CFA Petition at 6-7.

[117]Time Warner Opposition at 5.

[118]Liberty Media Reply at 5-9.

[119]NCTA Opposition at 7-8; NCTA Reply at 3-5.

of current Commission rules and statutes. Specifically, the public interest factors of Section 613 state that the Commission is to "take particular account of the market structure, ownership patterns, and other relationships of the cable television industry," "account for any efficiencies and other benefits that might be gained through increased ownership or control," "make such rules and regulations reflect the dynamic nature of the communications marketplace," and "not impose limitations which would impair the development of diverse and high quality video programming."[120]

50. Statutes and rules such as the program access, program carriage, channel occupancy limits, and must-carry requirements all affect the way the cable television industry currently operates and have a profound effect on current industry structure and performance. For example, in the *1994 Competition Report*, the Commission stated that, "[t]o the extent that large MSOs used their power over vertically-integrated programmers to obtain exclusive distribution rights to satellite-delivered programming, and those exclusive rights disadvantaged competitors of those large MSOs, the 1992 Cable Act's program access provisions and the Commission's program access rules appear to have largely addressed the problem."[121] In the *1997 Competition Report*, the Commission noted that "the program access rules have been credited as having been a necessary factor in the development of both the DBS [direct broadcast satellite] and MMDS [multichannel multipoint distribution service] industries."[122] Because these provisions have real and substantive impact upon the market, the Commission, in

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[120] 47 U.S.C. § 533(f)(2)(C), (D), (E), (G).

[121] *1994 Competition Report* at ¶ 149.

[122] *1997 Competition Report* at ¶ 230. *See also Second Report and Order* at ¶ 54 ("carriage of broadcast, PEG [public, educational, and governmental] and leased access channels promote diversity and provides alternative sources of unaffiliated programming to cable subscribers in furtherance of the statutory objectives"); *First Order on Reconsideration* at ¶ 27 (reaffirming same).

setting the horizontal ownership limit, may properly consider the impact of these provisions in alleviating some of the public interest and anticompetitive concerns about horizontal concentration.[123]

51. In addition to CME/CFA's argument that the Commission should not have placed any reliance on the impact of these other statutes and rules, both CME/CFA and Viacom argued that the Commission placed too much weight on the impact of these other statutes and rules on alleviating competitive concerns. In the *Second Report and Order*, the Commission recognized that anticompetitive concerns might indeed be present under the current market structure. The Commission did not conclude that statutory provisions and rules such as the program carriage and access provisions, the must-carry requirements, and the channel occupancy limits were sufficient by themselves to address anticompetitive concerns about horizontal concentration. The Commission did find that, when combined with these other statutory provisions and rules addressing similar concerns, the 30% horizontal ownership limit was "reasonable" and stated that: "The cumulative effect of these regulations coupled with a horizontal ownership limit of 30% should protect against any one cable system exerting undue power that could prevent the success of new video programming services or `unfairly impede the flow of video programming to the consumer.'"[124] The Commission's weighing of these other statutory provisions and rules in crafting the rules adopted in the *Second Report and Order* was appropriate.

B. Requests to Revise the Calculation Factors

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[123]To insure that our other rules have their continued efficacy, we have explored, where necessary, suitable adjustments to these rules. *See, e.g., Memorandum Opinion and Order and Notice of Proposed Rulemaking, In the Matter of Implementation of the Cable Television Consumer Protection and Competition Act of 1992, Petition for Rulemaking of Ameritech New Media, Inc. Regarding Development of Competition and Diversity in Video Programming Distribution and Carriage*, FCC 97-415, CS Docket no. 97-248, RM No. 9097 (rel. Dec. 18, 1997).

[124]*Second Report and Order* at ¶ 26 (quoting 47 U.S.C. § 533(f)(2)(A)).

1. Inclusion of Affiliated Telephone Companies

a. Background

52. CME/CFA requested that the Commission take into account in the calculation of "homes passed" the number of telephone households of a telephone company affiliated with an MSO. CME/CFA argued that the current regulations do not take into account proposed mergers and joint ventures between telephone companies and cable companies -- e.g., the (then) proposed merger of Bell Atlantic and TCI that would have resulted in access to 40% of all U.S. households, either through Bell Atlantic telephone lines or TCI's cable systems. CME/CFA argued that just as "homes passed" measures potential cable subscribers, telephone customers should be viewed as potential "cable subscribers" via video dialtone or broadband networks. CME/CFA argued that if cable and telephone companies merge, the potential for direct competition in their overlapping areas is removed and smaller video programmers are threatened.[125] CME/CFA further stated that its proposed expansion of the horizontal ownership rules is a logical outgrowth of the "homes passes" standard, as potential VDT subscribers are functionally indistinguishable from potential cable subscribers.[126]

53. MSOs and telephone companies uniformly responded that the Commission does not have the authority under Section 613 to treat telephone customers as "cable subscribers."[127] NCTA and Bell Atlantic argued that Section 613 specifically refers to "cable subscribers" reachable through "cable systems" and that VDT and other systems are

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[125]CME/CFA Petition at 11-13.

[126]CME/CFA Reply at 5-7.

[127]Time Warner Opposition at 9-10; TCI Opposition at 8; Liberty Media Opposition at 12-13; U S West Communications, Inc. Opposition to CME/CFA Petition at 1-3; GTE Service Corporation Opposition to CME/CFA Petition at 2; BellSouth Telecommunications, Inc. Opposition to CME/CFA Petition at 3-7; Bell Atlantic Opposition to CME/CFA Petition at 2-5.

not regarded as "cable services or systems" in their respective proceedings.[128] U S West Communications, Inc. ("U S West") argued that the Communications Act's definition of "cable system" specifically excludes common carrier facilities subject to Title II of the Communications Act.[129] In addition, Bell Atlantic argued that VDT service is not a single "facility" that includes the necessary signal generation, reception and control equipment required of a "cable system," since a VDT network's generation and transmission equipment will generally be provided by the programmers.[130] GTE Service Corporation ("GTE"), BellSouth Telecommunications, Inc. ("BellSouth") and Bell Atlantic also stressed that unlike cable, VDT is an open-access, subscriber controlled system where the subscriber will not be the programming captive of the telephone company, because the telephone company is a common carrier.[131] Liberty Media pointed out that the proposal ignores the Commission's rules prohibiting a telephone company from acquiring a cable system within its telephone service area.[132]

54. Time Warner argued that the CME/CFA proposal would discourage telephone investment in cable and would be fundamentally at odds with the Commission's "two wires" policy.[133] NCTA also stated that CME/CFA's proposition is absurd because it would require the Commission to consider all telephone subscribers as "potential cable customers" in determining the percentages.[134]

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[128]NCTA Opposition at 9-10; Bell Atlantic Opposition at 2-5.

[129]U S West Opposition at 2 (citing 47 U.S.C. § 522(7)).

[130]Bell Atlantic Opposition at 4.

[131]*Id.* at 4-5; GTE Opposition at 2; BellSouth Opposition at 5-7.

[132]Liberty Media Opposition at 12-13 (discussing 47 C.F.R. § 63.54(d)(3)).

[133]Time Warner Opposition at 9-10.

[134]NCTA Opposition at 9-10.

55. Bell Atlantic posited that the proposal would impose an arbitrary limit on the very companies capable of succeeding as new entrants against the cable companies and would provide a disincentive in creating and upgrading VDT services. According to Bell Atlantic, under its then proposed merger with TCI, Bell Atlantic would have upgraded TCI's systems to allow telephone service in competition with incumbent telephone companies. TCI would have divested itself of cable systems in Bell Atlantic's region and Bell Atlantic would have upgraded its networks to compete with these systems. Bell Atlantic noted that similar arrangements were included in other cable-telco transactions proposed at the time the comments were filed.[135]

56. Liberty Media also stated that since the Commission Notices in this docket did not mention potential application of the limits to telephone customers, to extend the limits would violate the Administrative Procedure Act ("APA").[136]

57. CME/CFA responded that the Commission always has the authority to regulate in ways "reasonably ancillary to the effective performance of the Commission's various responsibilities for the regulation of television broadcasting."[137] The Commission has authority under the "reasonably ancillary" test to achieve "long established" goals or "ultimate purposes."[138] CME/CFA asserted that, since the Commission had power before Section 613 to impose horizontal limits

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[135]Bell Atlantic Opposition at 5-8.

[136]Liberty Media Opposition at 12-13 (citing *National Black Media Coalition v. FCC*, 791 F.2d 1016, 1022-23 (2d Cir. 1986) (although final rule need not be an "exact replica of the rule proposed in the Notice," the Notice must be sufficient "to give the public advance notice of the scope of its proceedings")).

[137]CME/CFA Reply at 5-7 (quoting *United States v. Southwestern Cable Co.*, 392 U.S. 157, 178 (1968)).

[138]*Id.* (citing *Home Box Office, Inc. v. FCC*, 567 F.2d 9, 28 (D.C. Cir.), *cert. denied*, 434 U.S. 829 (1977)).

on the cable industry, the Commission certainly has authority to adopt limits which include affiliated telephone subscribers under the "reasonably ancillary" standard.[139] However, CME/CFA stated, that if the Commission finds that considerations of fairness and the APA require further rulemaking, the Commission should initiate such a procedure.

b. Discussion

58. Section 613 specifically authorizes the Commission to place limits on "cable subscribers" a person may reach through "cable systems."[140] Where the use of a telephone company's lines is limited to the provision of local exchange services, we see no reason why that company's telephone subscribers should be counted as cable subscribers for the purposes of the cable horizontal ownership limit.[141] Likewise, the cable horizontal ownership limit does not apply to subscribers of a telephone company that offers multichannel video programming distribution service solely through means other than a "cable system."[142]

59. We note, however, that if a telephone company offers multichannel video programming distribution service to subscribers through a "cable system," the households passed by that cable system would be regarded as "cable households" for purposes of the cable horizontal ownership rules.[143] As discussed below, the Commission

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[139]CME/CFA Reply at 7.

[140]NCTA Opposition at 9-10; Bell Atlantic Opposition at 2.

[141]We note that the proposed TCI-Bell Atlantic merger was never consummated.

[142]*See* 47 U.S.C. § 651 (setting forth options for telephone companies entering the video marketplace). We note that the Commission's VDT rules and policies were repealed by Section 302(b)(3) of the 1996 Telecommunications Act, Pub. L. No. 104-104, 110 Stat. 56.

[143]This standard is consistent with the current horizontal ownership limit, which is based on the cable system's potential reach, i.e., the number of homes

will be seeking further comment on possible revisions to the rules to take into account all MVPD subscribers, such that a person would be allowed to reach fewer subscribers through cable systems if that person also reaches a large percentage of MVPD subscribers nationwide through other MVPD systems, including video distribution by a telephone company.

2. Exemption for Systems Facing Effective Competition

a. Background

60. Bell Atlantic proposed that homes in franchise areas facing "effective competition" not be included in calculating whether an operator has reached the 30% limit.[144] To illustrate Bell Atlantic's proposal, assume that cable company A passed 25% of cable homes nationwide, but 5% of these cable households were in areas subject to "effective competition." Under Bell Atlantic's proposal, if 10% of the cable homes passed nationally were in franchise areas subject to "effective competition," cable company A's horizontal share under the rules would not be 25% but would be 22%.[145] Bell Atlantic argued that horizontal ownership limits are only required to combat the local monopoly and "gatekeeper" power of cable systems, so that the justification for these limits disappear where local distribution markets are

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passed. We note, however, that we are revisiting this issue under the *Further Notice of Rulemaking* and seek comment on the possibility of changing the method of calculating the horizontal ownership limit from potential reach to actual reach, i.e., the number of subscribers served.

[144]Bell Atlantic Petition at 1-2.

[145]To see how this result is reached, assume that 100 million homes are passed nationally, and cable company A serves 25 million of these. If 10% of the nation were in "competitive" markets, the number of households not subject to competition would be 90 million. Cable company A serves 20 million of these, resulting in a percentage of 20/90 or 22%.

competitive.[146]

61. Bell Atlantic argued that subjecting systems under "effective competition" to the horizontal ownership limits will harm competition in the industry. Bell Atlantic contends that, in exempting competitive markets from rate regulation, Congress recognized that competition eliminates the ability of cable operators in those markets to exercise market power and that continued regulatory constraints hinder flexibility in those markets. According to Bell Atlantic, Congress found that cable operators' ability to exercise market power arises from lack of competition in local service areas. As a result, Bell Atlantic asserts, national market power over programmers is diminished by the presence of competition at the local level.[147]

62. CME/CFA argued that Bell Atlantic's argument ignores Congress' well-founded concern that MSOs exercise market power at the national level by dint of sheer size.[148] Congress did not provide an "effective competition" exception here, as it did for rates in Section 3 of the 1992 Cable Act, indicating that Congress did not intend such an exception.[149] CME/CFA noted that Bell Atlantic provides no evidence that the presence of local competition diminishes the incentive or ability of cable operators to favor affiliated programmers and disfavor independents.[150] CME/CFA argued that it is not clear how sporadic local competition seriously undermines the power which flows from "being able to provide ready-made subscriber levels."[151] CME/CFA also pointed out that, because years and "billions of dollars" were

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[146]*Id.* at 2-5.

[147]*Id.* at 1-3, 4-6.

[148]CME/CFA Opposition to Bell Atlantic Petition at 3.

[149]*Id.*

[150]*Id.* at 4.

[151]*Id.* at 6-7.

required before VDT was to become operational, VDT systems at that time could not compete with cable or offer independent programmers a viable alternative to delivery by cable.[152] Since broadcasters are subject to analogous limits despite vigorous competition from local stations, CME/CFA stated that there is no reason for making local competition a basis for dropping the horizontal ownership limits on MSOs.[153]

63. Bell Atlantic responded to the CME/CFA opposition by stressing that it was not asking the Commission to eliminate the ownership limits where only a "theoretical" possibility of competition exists. Instead, Bell Atlantic argued, it simply proposed that these limits not apply where actual head-to-head competition exists. Where competition exists, according to Bell Atlantic, distributors have strong incentives to ensure that consumers obtain the programming they value, regardless of source. The only effect of applying these limits in competitive markets, Bell Atlantic contended, would be to prevent established companies from invading each others' territories and to inhibit entry by those companies that are best equipped to compete with existing MSOs.[154]

b. Discussion

64. We agree with Bell Atlantic that the concern that cable operators may "unfairly imped[e]. . . the flow of video programming from the video programmer to the consumer"[155] will be reduced when there is sufficient competition at the local distribution level. If there is sufficient local distribution competition, the local cable operator will no longer be a "gatekeeper" over that particular audience and video

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[152] *Id.* at 5.

[153] *Id.* at 8-9.

[154] Bell Atlantic Reply at 1-3.

[155] 47 U.S.C. § 533(f)(2)(A).

programmers would have alternative means to reach that audience.[156] We disagree with Bell Atlantic's conclusion that horizontal ownership limits are only required to combat the local monopoly of cable systems, so that the justification for these limits disappears where there is sufficient local competition to satisfy the "effective competition" standard applicable to rate deregulation.

65. A level of competition sufficient to support rate deregulation is not necessarily sufficient to address the public policy objectives of the horizontal ownership rules. As we observed in the *First Order on Reconsideration* in rejecting Bell Atlantic's similar argument in the context of channel occupancy limits, "the effective competition standard was not adopted for this specific purpose and [] it is not clear that the presence of effective competition for any cable system will address all of the relevant concerns that Congress expressed in enacting Section 11 of the 1992 Cable Act."[157] As an example, we noted that, if both the cable system and the competing MVPD are vertically integrated, unaffiliated programming services may continue to be denied access from either outlet, thus frustrating the diversity and competition objectives of the 1992 Act.[158] We agree with CME/CFA that, had Congress intended to eliminate all cable regulations where systems face effective competition, the effective competition exemption would have been drawn much more broadly. Instead, the exemption is expressly limited to rate regulation; nowhere in either its language or legislative history does it state that the presence of head-to-head local distribution competition will render the horizontal ownership rules unnecessary.[159]

66. The "effective competition" standard determines when

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[156] *See Second Report and Order* at ¶ 29.

[157] *First Order on Reconsideration* at ¶ 47.

[158] *Id.*

[159] *Id.* at ¶ 48.

there is sufficient local competition to prevent an incumbent cable operator from exercising market power in setting local rates for cable services sold to local subscribers. In contrast, the horizontal ownership limit was designed to ensure that no cable MSO acquires a sufficiently large share of subscribers nationwide to exercise undue market power at the national level in its purchase of programming from networks, which generally sell their programming nationwide.[160] In the *Second Report and Order*, the Commission rejected an argument similar to that of Bell Atlantic, stating: "The presence of effective competition in any given system or group of systems does not, however, directly respond to Congress' concern about the exercise of undue control by a single entity at the national level."[161] We reaffirm that decision today. We will not assume that, in their bargaining, programming networks and cable MSOs do not consider an MSO's total subscribership, but only its subscribers in areas not subject to "effective competition." There may be grounds for revising the 30% horizontal ownership limit, however, as more systems become subject to effective competition.

3. Attribution Rules

a. Background

67. CME/CFA asked that the Commission tighten its attribution rules by eliminating the single majority shareholder exception, which provides that minority interests will not be attributed where a single shareholder owns more than 50% of the outstanding voting stock.[162] CME/CFA argued that this exception to the attribution rules is "unduly mechanistic" and ignores the minority shareholder's "ability to influence the actual operation of the property" even when a majority shareholder is present. CME/CFA posited that there

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[160]*See Second Report and Order* at ¶ 29; *see also* 47 U.S.C. §§ 533(f)(2)(A), (B) & (C).

[161]*Id.*

[162]CME/CFA Petition at 22-23 (incorporating by reference CFA's September 1993 Reply Comments at 4-5).

are situations where a single majority shareholder may be forced to accommodate minority shareholders.

68. Responding to the CME/CFA proposal, NCTA noted that the attribution rules address the ability of an MSO to influence in a meaningful way the programming decisions of an individual cable system. NCTA argued that the single majority shareholder exception appropriately recognizes that the influence of non-majority shareholders is significantly attenuated when a majority shareholder exists, such that attribution is not required.[163]

b. Discussion

69. In the *Second Report and Order*, the Commission adopted the broadcast attribution rules, which contain the single majority shareholder exception,[164] in the cable horizontal ownership context because "the objectives of the broadcast attribution model are consistent with our goals in establishing ownership standards for subscriber limits."[165] The Commission explicitly stated that the broadcast rules "focus on ownership thresholds that enable a broadcast licensee to influence or control management or programming decisions" and that "these same issues are also relevant to addressing the concerns at issue in this proceeding relating to the ability of cable operators to unduly influence the programming marketplace.[166]

70. The Commission does not believe there is enough evidence in this docket to justify reversing our prior opinion that, in single majority shareholder situations, ownership of minority voting stock alone is unlikely to grant sufficient "influence" over programming decisions to warrant attribution. The single majority shareholder provision of the rules is currently under review in the broadcast

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[163]NCTA Opposition at 15-16.

[164]47 C.F.R. § 73.3555 n. 2(b).

[165]*Second Report and Order* at ¶ 35.

[166]*Id.* at ¶ 35.

context in MM Docket Nos. 94-150, 92-51 and 87-154.[167] In that proceeding, the Commission sought comment on the nature of "influence" and "control" and the connection between equity ownership and such influence and control. The Commission is also issuing a Notice of Proposed Rulemaking seeking comment on whether and how the cable attribution rules should be revised. Given the paucity of information in this proceeding from which to make an informed decision as to the need for changes in the attribution standards, that appears to be the preferable course.

71. This determination regarding the cable attribution rules applies to both our horizontal ownership rules and channel occupancy limits. As we noted in the *First Order on Reconsideration*,[168] that order addressed the issues on reconsideration regarding our cable channel occupancy limits, but left issues concerning the cable attribution standard for the current proceeding.

IV. MOTION TO LIFT STAY

a. Background

72. In the *Second Report and Order*, the Commission voluntarily stayed the effective date of the cable horizontal ownership rules pending final judicial resolution of the District Court decision in *Daniels* that the underlying statute violates the First Amendment.[169] While the *Daniels* Court had stayed further District Court proceedings

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[167] *See Notice of Proposed Rulemaking, In the Matter of Implementation of the Cable Television Consumer Protection and Competition Act of 1992, Review of the Commission's Cable Attribution Rules*, MM Docket Nos. 94-150, 92-51 and 87-154, FCC 94-324, 10 FCC Rcd 3606 (1995); *Further Notice of Proposed Rule Making, In the Matter of Implementation of the Cable Television Consumer Protection and Competition Act of 1992, Review of the Commission's Cable Attribution Rules*, MM Docket Nos. 94-150, 92-51 and 87-154, FCC 96-436, 11 FCC Rcd 19895 (1996).

[168] *Memorandum Opinion and Order on Reconsideration of the Second Report and Order* in MM Docket 92-264, FCC 95-147, 10 FCC Rcd 7364, n. 3 (1995).

[169] *Second Report and Order* at ¶ 109.

pending interlocutory appeal of its judgment, it had not enjoined the Commission from adopting and enforcing horizontal ownership rules under the statute.[170] CME/CFA filed a motion to lift the Commission's voluntary stay, which was opposed by NCTA.[171]

73. CME/CFA argued that, because the *Daniels* Court elected to stay further District Court proceedings pending appeal, the Commission's stay "cancels out the Court's stay, resulting in a situation where there are no regulations controlling the growth of cable systems while the constitutionality of the limits is being appealed."[172] As a result, CME/CFA argued, while stays are generally granted to preserve the status quo, the Commission's stay does not preserve the status quo.[173] CME/CFA further argued: (1) that the Commission and the United States are likely to prevail on the merits on appeal;[174] (2) that lifting the stay during the litigation will not result in irreparable harm to cable operators because the current rule still allows expansion for all cable systems and only causes "a temporary inability to expand beyond the 30% limit;"[175] (3) that continuance of the stay could result in harm to video programmers and the public;[176] and (4) that the public interest in "achieving competition and diversity in the cable television marketplace" requires that the rules be enforced while the constitutionality of the limits are under review.[177]

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[170] *Daniels*, 835 F.Supp. at 12.

[171] CME/CFA Motion to Lift Stay; NCTA Opposition to Motion to Lift Stay.

[172] CME/CFA Motion to Lift Stay at 1-2.

[173] *Id.* at 2.

[174] *Id.* at 2-4.

[175] *Id.* at 4.

[176] *Id.* at 4-6.

[177] *Id.* at 6.

74. In its opposition, NCTA argued that the case for a stay is one of "surpassing strength." NCTA stated: (1) that it is "far from clear" that the cable horizontal ownership limits will be upheld; (2) that "irreparable injury will result if cable systems are prevented from lawfully expanding their operations;" (3) that continuance of the stay during the litigation will not harm other interested parties, such as video programmers and the public; and (4) that the public interest favors the stay because the stay avoids "potential confusion and uncertainty during the period of judicial review."[178]

b. Discussion

75. In August 1996, the D.C. Circuit Court consolidated the *Daniels* appeal regarding the facial validity of the statute and the *Time Warner* challenge to the Commission's rules, and determined to hold court proceedings in abeyance while the Commission reconsidered the horizontal rules.[179] In light of the continuing pendency of the judicial proceedings relating to the underlying provision, we will retain the voluntary stay of the 30% horizontal ownership limit at this time.[180] That decision has been appealed and the Commission has argued that the provision in question is indeed constitutional.

76. In order to facilitate monitoring of MSOs' ownership interests, we will lift the stay insofar as it applies to the information submission provisions of 47 C.F.R. § 76.503(c) that are applicable when any person or entity holding an attributable interest in cable systems reaching 20% or more of homes passed nationwide acquires additional

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[178]NCTA Opposition to Motion to Lift Stay at 3.

[179]*Time Warner*, 93 F.3d at 979-80.

[180]Consumers Union/CFA filed a petition for rulemaking on September 23, 1997, requesting, among other things, that the Commission lift its voluntary stay. *Petition to Update Cable Television Regulations and Freeze Existing Cable Television Rates*, RM-9167, MM Docket Nos. 92-264, 92-265, 92-266, at 14-15 (filed Sept. 23, 1997) ("CU/CFA Petition for Rulemaking"). This *Second Order on Reconsideration* denies that particular request.

cable systems. The existing rules require a certification that no violation of the 30% limit will occur as a result of such acquisition. In light of the continuation of the stay, however, the certification should only specify the incremental change the acquisition makes in terms of the 30% of household passed standard, i.e. specifying the ownership in terms of homes passed before and after the acquisition is complete.

77. Affected parties will be required to come into compliance with the horizontal ownership rules within 60 days of the appellate court's issue of a mandate upholding Section 613(f)(1)(a) and the rules, unless the Commission determines as part of this ongoing proceeding to lift the stay at an earlier date. Interested parties, including in particular parties that are now entering into business arrangements that would violate the rules but for the existence of the stay, should be well aware of the existence of the rules and thus have a full opportunity to be prepared to comply with them.

V. FURTHER NOTICE OF PROPOSED RULEMAKING

78. We stated in the *Second Report and Order*, adopting the rules in question in this proceeding, that

> we plan to review subscriber limits every five years to determine whether such limits are reasonable under the prevailing market conditions and whether such limits continue to serve the objectives for which they were adopted. We regard such periodic review as an important means of addressing Congress' intent that such rules reflect the "dynamic nature of the communications marketplace."[181]

The rules in question were adopted in 1993, and it is appropriate that we undertake this review to address intervening changes in the communications marketplace. We seek comment on whether 30% remains the appropriate horizontal ownership limit in light of evolving market conditions. In addition, the current rules allow ownership of additional cable systems reaching up to 35% of cable homes passed, pro-

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[181] *Second Report and Order* at ¶ 40 (citing 47 U.S.C. § 533(f)(2)(E)).

vided such additional cable systems are minority-controlled.[182] The purpose of the minority-control allowance was to encourage diversity of viewpoints by fostering increased minority participation and ownership in the cable industry, through increased MSO investment in minority-owned cable systems.[183] Recognizing that the minority-control allowance has never been utilitized by any MSO, we seek comment on the effectiveness of this rule and on the development of alternative rules to serve our purpose of promoting minority participation. We also recognize that, since this rule was adopted, the Supreme Court issued *Adarand Constructors, Inc. v. Pena*, 515 U.S. 200 (1995). We seek comment on the constitutionality of the minority-control allowance in light of that decision. We also seek comment on how we can develop our policies consistent with the standards set forth in *Adarand*.

79. We also seek comment on two specific issues concerning the method of ownership calculation: (1) whether the rules should consider the presence in the market of all MVPDs rather than cable operators alone, and (2) whether the rules should be based on actual subscriber numbers rather than on homes passed.[184] The rules proposed here would provide that, in calculating a cable MSO's market share, the numerator would consist of the MSO's cable subscribers plus its non-cable MVPD subscribers, and the denominator would consist of the total number of cable subscribers plus non-cable MVPD subscribers nationwide. In addition to these proposed rule changes, we seek comment as to whether the method of ownership calculation should

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[182] 47 C.F.R. § 76.503(b).

[183] *Second Report and Order* at ¶ 28.

[184] The Commission also has issued a *Notice of Proposed Rulemaking, In the Matter of Streamlining of the Commission's Rules for the Direct Broadcast Satellite Service*, FCC 98-26, IB Docket No. 98-21 (rel. Feb. 26, 1998), requesting comment as to whether limitations on cable/DBS cross-ownership are necessary to address horizontal concentration in the MVPD market.

be modified in some way to support cable overbuild competition.

80. The MVPD market has continued to evolve since our adoption of the horizontal ownership rules. The *1997 Competition Report* noted the growth of MVPDs other than cable operators and suggested that a true measure of horizontal concentration ought to take into account all MVPDs and MVPD subscribers, rather than cable operators and cable subscribers alone:

> [I]n assessing the impact that national concentration may have in the MVPD programming market, we believe that it is appropriate to consider the presence of all MVPDs and MVPD subscribers in national concentration figures, and not just cable MSOs and cable subscribers. As non-cable MVPD subscribership increases, the significance of DBS, MMDS and SMATV operators in the MVPD program purchasing market also increases.[185]

With the growth of alternative MVPDs, network programmers gain alternative avenues for distribution of their products, thus reducing cable operators' market power or influence in the purchase and distribution of network programming. Conversely, just as growth in alternative MVPDs' subscribership can reduce a cable MSO's market power, a cable MSO also can increase its market power by acquiring interests in alternative MVPDs.

81. We seek comment on a proposal to revise the rules to include alternative MVPDs in the measure of horizontal concentration in order to reflect the emergence of competitors to cable in the video marketplace, as well as potential MSO increases in market power through acquisition of interests in other MVPDs. By recognizing the impact of all purchasers of video programming, not just cable operators, this rule revision would provide a more accurate measure of MSOs' market power.

82. We seek comment on whether the proposed revision of

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[185] *1997 Competition Report* at ¶ 150.

the horizontal ownership rules is consistent with the Commission's authority under Section 613 of the Communications Act to "prescribe rules and regulations establishing reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems . . .."[186] This proposal would result in a sliding or adjustable cable horizontal ownership limit, under which the number of subscribers a cable operator is authorized to reach through cable systems would decrease in proportion with any increase in the number of subscribers that entity reaches through other MVPD systems. Conversely, the cable horizontal ownership limit would rise for a cable operator that reaches fewer subscribers through other MVPD systems. The proposed rules would impose no limit on the number of subscribers a cable operator may reach through alternative MVPD systems. These rules also would not apply to persons who have no attributable ownership interests in cable systems. We seek comment on this proposal and on whether it is consistent with the terms of the underlying statute, given Section 613's focus on the cable industry and the establishment of a cable subscribership limit rather than an MVPD subscribership limit.

83. We also seek comment on the possibility of changing the method of calculating the basis of the horizontal ownership limits from potential reach, i.e., number of homes passed, to actual reach, i.e., number of MVPD subscribers served. In the *Second Report and Order*, we stated that the homes passed standard reflects a cable operator's potential reach and constitutes a more stable basis on which to impose horizontal limits than a subscriber based standard.[187] We also noted some commenters' argument that a subscriber based standard may have the effect of discouraging subscriber growth.[188] In revisiting the horizontal ownership rules, we seek comment on whether the homes

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[186]47 U.S.C. § 533(f)(1)(A).

[187]*Id.* at ¶ 24.

[188]*Id.* at ¶ 19.

passed standard continues to be an accurate measure of horizontal concentration and market power in today's marketplace, and whether the easier to measure subscriber standard can be adapted for use in a fashion that will not require an abrupt halt to the addition of new subscribers to established cable systems.

84. While homes passed reflect the number of subscribers an MVPD has the potential of reaching, the MVPD often secures only a fraction of those potential subscribers. The MVPD typically does not purchase programming for all potential subscribers, only for those subscribers that it actually has. As alternative MVPDs continue to grow in the future, the number of homes passed by a cable operator may become an increasingly inaccurate measure of its actual subscribership and thus of its actual market power. We seek comment on whether the ownership calculation should be based on the number of actual subscribers, rather than homes passed, in order to reflect an MVPD's actual purchasing power.

85. The homes passed standard is also difficult to apply if we revise the horizontal ownership rules to consider all MVPDs in the calculation, since several different MVPDs may pass the same homes. Furthermore, the homes passed standard is a particularly inaccurate measure of market power for a new MVPD whose actual subscribership is only a small fraction of its potential reach in terms of homes passed. For example, under a homes passed standard, each direct to home satellite service provider, no matter how weak or new an entrant, could be deemed to pass virtually all homes in the country and thus be deemed to have far greater market power than an established cable operator passing 30% of homes nationwide. We ask commenters to comment on the best method for counting subscribers, including those residing in multi-dwelling units and commercial subscribers such as hotels, bars, etc.

86. We seek comment on whether the greater accuracy provided by a subscriber based standard outweighs the greater stabil-

ity provided by a homes passed standard. With regard to the argument that a subscriber based standard may have the effect of discouraging subscriber growth, we seek comment on whether system operators would have a sufficient opportunity to anticipate the approaching limit and to dispose of systems sufficient to stay under the limit rather than to simply cease the addition of new subscribers.

87. We ask commenters to address whether these proposed revisions will serve the public interest objectives that Congress directed the Commission to consider and balance in implementing the horizontal ownership limits, particularly the objectives "to ensure that no cable operator or group of cable operators can unfairly impede the flow of video programming from the programmer to the consumer;"[189] "to ensure that cable operators do not favor affiliated video programmers in determining carriage . . .;"[190] "to take account of the market structure, ownership patterns, and other relationships of the cable industry, including the market power of the local franchise . . .;"[191] and "to make rules and regulations that reflect the dynamic nature of the communications marketplace."[192]

88. We ask commenters to address whether the proposed revisions are consistent with the Commission's legal authority under Section 613 and other provisions of the Act[193] and are reasonable and appropriate given our objectives. We seek comment on whether the proposed horizontal ownership rules would provide a more accurate measure of horizontal concentration and market power than the current rules. We also seek comment on the practical impact of the

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[189]47 U.S.C. § 533(f)(2)(A).

[190]47 U.S.C. § 533(f)(2)(A).

[191]47 U.S.C. § 533(f)(2)(C).

[192]47 U.S.C. § 533(f)(2)(E).

[193]*See, e.g.*, 47 U.S.C. §§ 151, 154, and 303.

proposed rule changes on MSO ownership and operation. In particular, we ask that commenters address whether the proposed changes would place any cable MSO in violation of the 30% horizontal ownership limit and to provide specific factual information in support of any such conclusions. We seek comment on whether we should develop special rules to address situations where a cable MSO may exceed the 30% limit as a result of subscriber growth within an existing area of homes passed. We further invite comment on any other matters relevant to our proposals and tentative conclusions.

VI. INITIAL REGULATORY FLEXIBILITY ANALYSIS

89. As required by Section 603 of the Regulatory Flexibility Act, 5 U.S.C. § 603 ("RFA"), the Commission is incorporating an Initial Regulatory Flexibility Analysis ("IRFA") of the expected impact on small entities of any policies or proposals contained in this *Further Notice of Proposed Rulemaking* ("*Further Notice*"). Written public comments concerning the effect of the proposals in the *Further Notice*, including the IRFA, on small businesses are requested. Comments must be identified as responses to the IRFA and must be filed by the deadlines for the submission of comments in this proceeding. The Secretary shall send a copy of this *Further Notice*, including the IRFA, to the Chief Counsel for Advocacy of the Small Business Administration in accordance with paragraph 603(a) of the Regulatory Flexibility Act.[194] In addition, this *Notice* and IRFA will be published in the Federal Register.[195]

A. Need for, and Objectives of, the Proposed Rules

90. The 1992 Cable Act and subsequent actions to implement it, and Section 11(c) of the 1992 Cable Act in particular, are intended to encourage competition in the cable industry and prevent the exercise of undue market power by large cable multiple systems owners. The Commission issues this *Further Notice* to obtain comment

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194 5 U.S.C. § 603(a).

195 *See id.*

on whether certain aspects of the Commission's horizontal ownership rules should be revised to make them more effective in serving the public interest objectives Congress charged the Commission with protecting in Section 11(c).

B. Legal Basis

91. Authority for the actions proposed in this *Further Notice* may be found in Sections 1, 4, 303, and 613 of the Communications Act of 1934, *as amended*, 47 U.S.C. §§ 151, 154, 303, 533.

C. Description and Estimate of the Number of Small Entities to Which the Proposed Rules Will Apply

92. The RFA generally defines "small entity" as having the same meaning as the terms "small business," "small organization," and "small governmental jurisdiction" and "the same meaning as the term 'small business concern' under the Small Business Act unless the Commission has developed one or more definitions that are appropriate for its activities.[196] A small business concern is one which: (1) is independently owned and operated; (2) is not dominant in its field of operation; and (3) satisfies any additional criteria established by the Small Business Administration ("SBA").[197] Pursuant to 5 U.S.C. § 601(3), the statutory definition of a small business applies "unless an agency after consultation with the Office of Advocacy of the SBA and after opportunity for public comment, establishes one or more definitions of such term which are appropriate to the activities of the agency and publishes such definition(s) in the Federal Register."[198]

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196 5 U.S.C. § 601(3) (incorporating by reference the definition of "small business concern" in 15 U.S.C. § 632).

197 15 U.S.C. § 632.

198 While we tentatively believe that the SBA's definition of "small business" greatly overstates the number of cable entities that are small businesses and is not suitable for purposes of determining the impact of any proposals on small cable entities, for purposes of this *Notice*, we utilize the SBA's definition in determining the number of small businesses to which

93. The SBA has developed a definition of small entities for cable and other pay television services under Standard Industrial Classification 4841 (SIC 4841), which covers subscription television services, which includes all such companies with annual gross revenues of $11 million or less.[199] This definition includes cable systems operators, closed circuit television services, direct broadcast satellite services, multipoint distribution systems, satellite master antenna systems and subscription television services. According to the Census Bureau, there were 1,323 such cable and other pay television services generating less than $11 million in revenue that were in operation for at least one year at the end of 1992.[200]

94. The Commission has developed its own definition of a "small cable company" and "small system" for the purposes of rate regulation. Under the Commission's rules, a "small cable company," is one serving fewer than 400,000 subscribers nationwide.[201] Based on our most recent information, we estimate that there were 1,439 cable

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proposed rules would apply. However, we reserve the right to adopt a more suitable definition of "small business" as applied to cable or other entities subject to our rules, and to further consider in the future the number of existing small cable entities.

199 13 C.F.R. §121.201.

200 1992 Census, *supra*, at Firm Size 1-123. *See Memorandum Opinion and Order and Notice of Proposed Rule Making, Implementation of Sections of the Cable Telecommunications Consumer Protection and Competition Act of 1992, Rate Regulation and Cable Pricing Flexibility,* MM Docket No. 92-266 and CS Docket No. 96-157, 11 FCC Rcd 9517, 9531 (1996).

201 47 C.F.R. § 76.901(e). The Commission developed this definition based on its determinations that a small cable company is one with annual revenues of $100 million or less. *Sixth Report and Order and Eleventh Order on Reconsideration, Implementation of Sections of the 1992 Cable Act: Rate Regulation,* MM Docket Nos. 92-266 & 93-215, 10 FCC Rcd 7393 (1995).

companies that qualified as small cable companies at the end of 1995.[202] Since then, some of those companies may have grown to serve over 400,000 subscribers, and others may have been involved in transactions that caused them to be combined with other cable companies. Consequently, we estimate that there are fewer than 1,439 small entity cable companies that may be affected by the proposal adopted in this *Notice*. The Commission's rules also define a "small system," for the purposes of cable rate regulation, as a cable system with 15,000 or fewer subscribers.[203] We do not request nor do we collect information concerning cable systems serving 15,000 or fewer subscribers and thus are unable to estimate at this time the number of small cable systems nationwide.

95. The Communications Act also contains a definition of a "small cable operator," which is "a cable operator that, directly or through an affiliate, serves in the aggregate fewer than 1 percent of all subscribers in the United States and is not affiliated with any entity or entities whose gross annual revenues in the aggregate exceed $250,000,000."[204] The Commission has determined that there are 61,700,000 subscribers in the United States. Therefore, we found that an operator serving fewer than 617,000 subscribers is deemed a small operator, if its annual revenues, when combined with the total annual revenues of all of its affiliates, do not exceed $250 million in the aggregate.[205] Based on available data, we find that the number of cable operators serving 617,000 subscribers or less totals 1,450.[206] Although

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202 Paul Kagan Associates, Inc., *Cable TV Investor*, Feb. 29, 1996 (based on figures for Dec. 30, 1995).

203 47 C.F.R. § 76.901(c).

204 47 U.S.C. § 543(m)(2).

205 47 C.F.R. § 76.1403(b).

206 Paul Kagan Associates, Inc., *Cable TV Investor*, Feb. 29, 1996 (based on figures for Dec. 30, 1995).

it seems certain that some of these cable system operators are affiliated with entities whose gross annual revenues exceed $250,000,000, we are unable at this time to estimate with greater precision the number of cable system operators that would qualify as small cable operators under the definition in the Communications Act. We are likewise unable to estimate the number of these small cable operators that serve 50,000 or fewer subscribers in a franchise area.

D. Description of Projected Recording, Record keeping, and Other Compliance Requirements

96. If our horizontal ownership rules are changed, the Commission may have to change certain cable reporting requirements. Cable entities also may have to adjust the organization of their business interests in order to comply with any new rules that we may adopt.

E. Steps Taken to Minimize Significant Economic Impact on Small Entities, and Significant Alternatives Considered

97. The actions proposed in the *Further Notice* are intended to ensure that the Commission's horizontal ownership rules are effective in preventing the exercise of undue market power by large cable multiple systems owners and promote a competitive, diverse and fair marketplace. Accordingly, as discussed in the above descriptions of the proposed rule changes, the approaches proposed in this *Further Notice* should promote fairness and diversity for all cable systems, including the small entities listed above. We invite comments on these approaches, including comment on whether alternative approaches will mitigate any unwarranted expenses incurred by smaller entities by virtue of their size alone.

F. Federal Rules that Overlap, Duplicate or Conflict with the Proposed Rules

98. None.

VII. PAPERWORK REDUCTION ACT

99. The proposals contained herein in the *Further Notice* have been analyzed with respect to the Paperwork Reduction Act of 1995 (the "1995 Act") and found to impose modified information collection requirements. Implementation of any new or modified

requirements will be subject to approval by the Office of Management and Budget ("OMB"). The Commission, as part of its continuing effort to reduce paperwork burdens, invites the general public to take this opportunity to comment on the information collection requirements contained in this *Further Notice*, as required by the 1995 Act. Comments should address: (1) whether the proposed collection of information is necessary for the proper performance of the functions of the Commission, including whether the information shall have practical utility; (2) the accuracy of the Commission's burden estimates; (3) ways to enhance the quality, utility, and clarity of the information collected; and (4) ways to minimize the burden of the collection of information on the respondents, including the use of automated collection techniques or other forms of information technology.

100. Written comments by the public on the modified information collection requirements are due 45 days from date of publication of this *Second Order on Reconsideration and Further Notice* in the Federal Register. OMB comments are due 60 days from the date of publication in the Federal Register. Comments on the information collection requirements contained herein should be submitted to Judy Boley, Federal Communications Commission, Room 234, 1919 M Street, N.W., Washington, DC 20554, or via the Internet to jboley@fcc.gov and to Timothy Fain, OMB Desk Officer, 10236 NEOB, 725 - 17th Street, N.W., Washington, DC 20503 or via the Internet to fain_t@al.eop.gov. For additional information on the information collection requirements, contact Judy Boley at 202-418-0214 or via the Internet at the above address.

VIII. PROCEDURAL PROVISIONS

101. *Ex parte Rules - "Permit-but-Disclose" Proceeding*. This proceeding will be treated as a "permit-but-disclose" proceeding subject to the "permit-but-disclose" requirements under Section 1.1206(b) of the rules.[207] Ex parte presentations are permissible if disclosed in accordance with Commission rules, except during the Sunshine Agen-

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[207] 47 C.F.R. § 1.1206(b), as revised.

da period when presentations, ex parte or otherwise, are generally prohibited. Persons making oral ex parte presentations are reminded that a memorandum summarizing a presentation must contain a summary of the substance of the presentation and not merely a listing of the subjects discussed. More than a one or two sentence description of the views and arguments presented is generally required.[208] Additional rules pertaining to oral and written presentations are set forth in Section 1.1206(b).[209]

102. *Filing of Comments and Reply Comments.* Pursuant to applicable procedures set forth in Sections 1.415 and 1.419 of the Commission's Rules,[210] comments are due August 14, 1998, and reply comments are due September 3, 1998. To file formally in this proceeding, you must file an original plus four copies of all comments, reply comments, and supporting comments. If you want each Commissioner to receive a personal copy of your comments, you must file an original plus nine copies. You should send comments and reply comments to Office of the Secretary, Federal Communications Commission, 1919 M Street, NW, Washington, DC 20554. Comments and reply comments will be available for public inspection during regular business hours in the FCC Reference Center, Room 239, Federal Communications Commission, 1919 M Street NW, Washington DC 20554.

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[208] *See* 47 C.F.R. § 1.1206(b)(2), as revised.

[209] 47 C.F.R. § 1.1206(b).

[210] 47 C.F.R. §§ 1.415 and 1.419.

IX. ORDERING CLAUSES

103. Accordingly, IT IS ORDERED that the petitions for reconsideration filed in this proceeding ARE DENIED.

104. IT IS FURTHER ORDERED that the Motion to Lift Stay filed December 15, 1993 by the Center for Media Education and Consumer Federation of America IS GRANTED as to the Commission's voluntary stay on enforcement of 47 C.F.R. § 76.503(c), and IS DENIED as to the Commission's voluntary stay on enforcement of 47 C.F.R. §§ 76.503(a), (b), (d), (e) and (f).

105. IT IS FURTHER ORDERED that, pursuant to Sections 1, 4, 303 and 613 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154, 303 and 533, NOTICE IS HEREBY GIVEN of proposed amendments to the Commission's rules, in accordance with the proposals, discussions and statements of issues in the *Further Notice of Proposed Rulemaking*, and COMMENT IS SOUGHT regarding such proposals, discussions and statements of issues.

106. IT IS FURTHER ORDERED that the Commission SHALL SEND a copy of this *Report and Order and Second Further Notice of Proposed Rulemaking*, including the Initial Regulatory Flexibility Analyses, to the Chief Counsel for Advocacy of the Small Business Administration.

FEDERAL COMMUNICATIONS COMMISSION

Magalie Roman Salas
Secretary

Separate Statement of Commissioner Harold Furchtgott-Roth

In re: Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992, Horizontal Ownership Limits, *Second Memorandum Opinion and Order and Further Notice of Proposed Rulemaking*.

I am pleased that the Commission seeks comment on the constitutionality of the 35% "minority-control allowance," 47 CFR section 76.503(b), for cable subscriber limits. *See supra* at 32. In my view, the constitutionality of this provision in light of intervening judicial decisions – most notably, *Adarand v. Pena*, 515 U.S. 200 (1995) – is, at best, dubious.

Accordingly, while it certainly does no harm to seek comment on the efficacy of this regulation, I believe that such comment is entirely unnecessary and I would not have sought it. If a regulation appears to violate the Constitution, that is all we need to know in order to decide whether to affirm it on reconsideration.

At the outset, I note that the Commission's statutory authority to promulgate the minority-control allowance (or any other race-based cable subscriber limits, for that matter) is scant. Section 613(f)(1)(a), which orders the Commission to set horizontal ownership rules, is *entirely race-neutral*. Its plain language supports no rational inference that Congress intended different subscriber limits to apply to different people based on nothing other than their race:

> "[T]he Commission shall . . . prescribe rules and regulations establishing reasonable limits on the number of cable subscribers *a person* is authorized to reach through cable systems owned by *such person*, or in which *such person* has an attributable interest."

47 U.S.C. section 613(f)(1)(a)(emphasis added).

Nor do the "public interest" factors that Congress outlined make any distinctions between people based on minority or non-minority status. *See id.* section 613(f)(2)(A)-(G). To be sure, one of the factors states that the Commission shall "not impose limitations which would impair the development of diverse and high quality program-

ming." Section 613(f)(2)(G). Congress clearly meant for the Commission to protect cable operators' ability to show a wide variety of choice programming by not setting subscriber limits so low as to dry up concentration-based efficiencies that facilitate costly programming investments. *See* House Report at 43; Senate Report at 33; *see also* 8 FCC Rcd at 8571 (observing that "higher concentration levels enable[] cable companies to take advantage of economies of scale and foster investment in more and better original programming and a wealth of viewing options for consumers"). But there is no indication in the statute, or even its legislative history, that Congress meant for the Commission to view the issue of subscriber limits and varied, quality programming through the historically troubled lens of race.

In short, we simply do not have a clear Congressional directive that the Commission, in setting horizontal limits, make race-based distinctions among cable system owners. Given the weighty constitutional issues that arise whenever government employs such classifications, we should be reluctant to read them into statutes. *See generally United States v. Thirty-Seven Photographs*, 402 U.S. 363, 369 (1971) (statutes should be construed to avoid, not to create, constitutional problems).

II.

Section 76.503(b), which on its face employs racial classifications, raises grave constitutional questions. In particular, *Adarand v. Pena*, 515 U.S.200 (1995), which was decided after the Commission promulgated section 76.503(b), casts substantial doubt upon its constitutionality under the Equal Protection component of the Fifth Amendment.

In *Adarand*, the Supreme Court held that *all* governmental action based on race is subject to strict scrutiny. *Id.* at 226. This standard of review obtains, the Court made clear, whether or not the government's motives can be characterized as "benign." *Id.* at 227. Thus, the use of racial classifications by any governmental actor is now constitutionally permissible only where the measure is narrowly

tailored to serve a compelling government interest. *Id.* at 235.[1]

With respect to the government interest in section 76.503(b), the Supreme Court has never held that diversity of programming -- the Commission's purported goal in adopting the minority-control allowance, *see* 8 FCC Rcd 8565, 8578-79 (1993) -- qualifies as a compelling government interest. *See Lutheran Church-Missouri Synod v. FCC*, No. 97-1116, slip op. at 20-21 (D.C. Cir. April 14, 1998) (observing that in *Metro Broadcasting, Inc. v. FCC*, 497 U.S. 547 (1990), the Court held programming diversity to be an important but not a compelling government interest). There is simply no affirmative authority for the proposition that the interest that has been asserted by the Commission in support of its regulation is legally sufficient under strict scrutiny.[2]

Furthermore, as in other contexts, the Commission's stated goal is something of a moving target. The Second Report & Order adopting the allowance does not explain what the Commission actually intends

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[1]As an initial matter, this regulation plainly requires the government to engage in race-based decisionmaking. In situations where a cable operator has more than 30% but less than 36% of national subscribers, the question whether that person is within legal limits for subscribership depends entirely on the racial identity of those who own or control affiliated systems. Therefore, whatever claims might be advanced with respect to the applicability of *Adarand* to other Commission regulations, *cf. Lutheran Church-Missouri Synod v. FCC*, No. 97-1116, slip op. at 13 (D.C. Cir. April 14, 1998) (summarizing and rejecting argument that FCC's equal employment opportunity rules do not involve race-based decisionmaking), it cannot be maintained that government action under this regulation does not turn expressly and precisely upon considerations of race.

[2]In fact, this legal problem -- *i.e.*, the lack of a compelling government interest -- would arise with respect to any regulation created in order to foster programming diversity. I thus find it hard to see how any horizontal ownership rule intended to advance such a goal could be fashioned under *Adarand*, as the Commission suggests. *See supra* at 32 ("We seek comment on how we can develop our policies consistent with the standards set forth in *Adarand*").

to accomplish when it speaks of promoting "diversity" in cable programming. *Cf. id.* at 19 ("The Commission never defines exactly what it means by 'diverse programming.'"). Of course, were "diversity" defined in a content-specific way, such an interpretation would trigger the First Amendment, as the D.C. Circuit has noted. *See id.* at 19-20 ("Any real content-based definition of the term may well give rise to enormous tensions with the First Amendment.").[3]

With respect to the second step under strict scrutiny, the fit between the means and ends here is loose, if not sloppy. The Commission has stated that the 5% allowance will foster investment in minority-owned cable systems, in turn create more minority ownership, and ultimately result in more minority "viewpoints" in programming. *See* 8 FCC Rcd at 8578-79. But the record in this proceeding is devoid of any evidence to support the Commission's predictive rationale, particularly the assumption that cable system ownership by a person of a certain race will lead to an identifable type of programming content. *Cf. Lutheran Church*, slip op. at 22-23 (faulting Commission, in overturning EEO rules as unconstitutional, for lack of evidence "linking low-level employees [at broadcast stations] to programming content"); *Lamprecht v. FCC*, 958 F.2d 382 (D.C. Cir. 1992) (criticizing Commission, in finding gender preferences in licensing hearings unconstitutional, for lack of evidence of connection between female ownership of broadcast stations and "female programming").

Nor has the Commission made any attempt to explain why a 5% allowance is a more appropriate remedy for the posited diversity problem than a more limited allowance of, say, 3%. To the contrary, the flat 5% of extra passage for minority-controlled systems seems an exceedingly blunt instrument for achieving the Commission's goal

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In contrast to broadcasters, cable operators receive full First Amendment protection with respect to their transmission and selection of programming. *See Turner Broadcasting System, Inc. v. FCC*, 512 U.S. 622, 636-41 (1994). Accordingly, the First Amendment "tensions" referred to in *Lutheran Church*, which involved broadcasting, would be even stronger here.

(even if that goal were a legally compelling one, which, under current precedent, it is not). For instance, I can find no connection in the record between the particular percentage of extra subscribers that minority-controlled companies may serve under this regulation and the degree to which that allowance furthers ownership and programming. The 5% allowance thus appears to be a rigid numerical preference, with no record evidence to support either its necessity or efficacy in relation to the purported goal.

Relatedly, there appears to have been no consideration in this docket of race-neutral alternatives for increasing minority ownership or programming participation, as required under the narrow-tailoring prong of strict scrutiny. *See Adarand*, 500 U.S. at 237-38 (citing *Richmond v. J.A. Croson*, 488 U.S. 469, 507 (1989)). The Commission seems to have approached the use of this explicit racial classification as a foregone conclusion, rather than as an alternative approach after first evaluating the utility of rules that do not draw lines among citizens based on their race. Indeed, in the notices of proposed rulemaking and the order of adoption, the Commission never even broached the possibility of race-neutral rules. *See* 8 FCC Rcd 210, 217 n. 58 (1992); 8 FCC Rcd 6828, 6850-51 (1993); 8 FCC Rcd at 8678-79. This is perhaps understandable given that *Adarand* had not been decided at the time these documents were issued, but that fact does not solve the basic deficiency in this proceeding that now exists under that case.

III.

For the foregoing reasons, governing judicial precedent strongly suggests that section 76.503(b), which literally creates two sets of rules for regulated entities based solely on the racial identity of those who own or control related systems, constitutes a denial of equal protection of the laws. The Commission has failed to articulate either a compelling government interest or to achieve a carefully crafted fit between the means it has chosen and the ends it says it intends to promote. The regulation therefore appears to be, at this juncture, facially unconstitutional.

* * *

As indicated above, I certainly cannot object to my fellow Commissioners asking questions about the practical workings of the rule. The significance of such information, however, pales in comparison to the strong indication under existing caselaw that the regulation is unconstitutional. As the courts have admonished us, "[f]ederal officials are not only bound by the Constitution, they must also take a specific oath to support and defend it." *Meredith Corp. v. FCC*, 809 F.2d 863, 874 (D.C. Cir. 1987). If a regulation appears to be unconstitutional, I believe that is reason enough -- indeed, it is the most important reason that I can imagine -- to eliminate the rule.

PARTIAL DISSENT OF COMMISSIONER GLORIA TRISTANI

In the Matter of Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992 -- Horizontal Ownership Limits, MM Docket No. 92-264

I would have lifted the Commission's voluntary stay on the enforceability of the horizontal ownership rules. In 1993, when the stay was imposed, a stay may have made sense: the largest cable operator, TCI, still controlled significantly less than 30% of cable subscribers nationwide and appellate review of the *Daniels* decision could have been expected well before the horizontal limit was threatened. In the past five years, that situation has changed dramatically. By the middle of 1997, TCI controlled 29.3% of cable subscribers, and with the flurry of deals announced over the last several months, it is clear that TCI has breached, or will soon breach, the 30% limit. Moreover, the anticipated appellate review never happened and may not happen anytime soon -- the D.C. Circuit has been waiting for the Commission to release this reconsideration of our rules before examining the underlying statute's constitutionality.

Under these circumstances, the 30% limit we are reaffirming today may be rendered moot unless the stay is lifted. To the extent that TCI already exceeds the 30% limit, I would identify those cases and address them separately. That task may be difficult, but not nearly as difficult as the situation we will face if TCI's dealmaking continues and a year from now the D.C. Circuit upholds the statute. Then we will face a situation in which the "facts on the ground" may severely hamper our ability to implement the right policy.

I recognize that the majority has put cable operators on notice that they must be prepared to come into compliance within 60 days if our rules are upheld. I am supportive of such an admonishment, but I am not convinced that it will be enforced. I therefore dissent on this part of the item.

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Supreme Court, U.S.
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NO. _____ OFFICE OF THE CLERK

IN THE

Supreme Court of the United States

TIME WARNER ENTERTAINMENT COMPANY, L.P., *et al.*,
Petitioners,

v.

FEDERAL COMMUNICATIONS COMMISSION AND
UNITED STATES OF AMERICA,
Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

PETITIONERS' APPENDIX
Volume II Pages 182-342

FERNANDO BOHORQUEZ, JR.
ANGELA J. CAMPBELL
INSTITUTE FOR PUBLIC REPRESENTATION,
GEORGETOWN UNIVERSITY LAW CENTER
600 New Jersey Ave., NW
Suite 312
(202) 662-9535

ANDREW JAY SCHWARTZMAN
(Counsel of Record)
CHERYL A. LEANZA
HAROLD J. FELD
MEDIA ACCESS PROJECT
950 18TH ST., SUITE 220
Washington, D.C. 20006
(202) 232-4300

Counsel for Consumer Federation of America, et al.

August 2, 2001

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IN THE MATTER OF IMPLEMENTATION OF THE
CABLE TELEVISION CONSUMER PROTECTION
AND COMPETITION ACT OF 1992
CS Docket No. 98-82

IMPLEMENTATION OF CABLE ACT REFORM PROVISIONS
OF THE TELECOMMUNICATIONS ACT OF 1996
Review of the Commission's Cable Attribution Rules
CS Docket No. 96-85

REPORT AND ORDER
FCC 99-288
Adopted: October 8, 1999
Released: October 20, 1999

By the Commission: Commissioner Furchtgott-Roth concurring in part, dissenting in part and issuing a statement; Commissioner Tristani approving in part, dissenting in part and issuing a statement.

I. Introduction

1. This *Report and Order* resolves the issues presented for comment in the *Notice of Proposed Rulemaking* ("*Cable Attribution Notice*") in this proceeding[1] as well as two related issues raised in the *Cable Reform Notice*.[2] In the *Cable Attribution Notice*, we initiated a review of our cable attribution rules, which define what constitutes an "attributable" or "cognizable interest" that triggers application of various Commission

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[1] *Notice of Proposed Rulemaking*, CS Docket 98-32, FCC 98-112 (rel. June 26, 1998) ("*Cable Attribution Notice*").

[2] *In re Implementation of Cable Act Reform Provisions of the Telecommunications Act of 1996, Order and Notice of Proposed Rulemaking*, CS Docket No. 96-85, 11 FCC Rcd 5937 (1996) ("*Cable Reform Notice*").

rules relating to the provision of cable television services (the "substantive cable rules"). In this *Report and Order*, we adopt amendments that will more accurately identify interests that confer on their holders the ability to influence or control the operations of the held entity or create the type of economic incentives that the substantive cable rules are intended to address. In this regard, our amendments to the cable attribution rules mirror to a certain extent those amendments we recently made to the broadcast attribution rules; thus, our reasoning herein largely incorporates and reiterates the reasoning set forth in the *Broadcast Attribution Report and Order*.[3]

II. Background

A. The Cable Attribution Rules

2. A variety of statutory provisions and Commission rules govern the conduct of cable television system operators or other entities in terms of both ownership interests that they may hold in other cable operators or competitive firms, or in terms of their conduct when they own, are owned by, or are owned in common with a "video programmer," a "satellite cable programming provider," or with other entities. For each of these statutory provisions or rules it is necessary to identify what types of ownership interests or other relationships are sufficient that

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[3] *See Regulations Governing Attribution of Broadcast and Cable/MDS Interests, Regulation and Policies Affecting Investment in the Broadcast Industry and Reexamination of the Commission's Cross-Interest Policy*, MM Docket Nos. 94-150, 92-51 and 87-154, *Report and Order* (rel. Aug. 6, 1999) ("*Broadcast Attribution Report and Order*"). The Broadcast Attribution Report and Order was issued after two notices for comment were issued. See *Notice of Proposed Rule Making, Review of the Commission's Regulations Governing the Attribution of Mass Media Interests*, MM Docket Nos. 94-150, 92-51 and 87-154, FCC 94-324, 10 FCC Rcd 3606 (1995) ("*Broadcast Attribution Notice*"); *Further Notice of Proposed Rule Making, Regulations Governing Attribution of Broadcast and Cable/MDS Interests, Regulation and Policies Affecting Investment in the Broadcast Industry and Reexamination of the Commission's Cross-Interest Policy*, MM Docket Nos. 94-150, 92-51 and 87-154, FCC 96-436, 11 FCC Rcd 19895 (1996) ("*Broadcast Attribution Further Notice*").

two legally separate entities should be treated as if they were commonly owned or managed or subject to significant common influence. The rules define that level of interest that brings the substantive statutory provision or rule in play to be an "attributable interest." Thus, for example, the Communications Act, Section 613(f)(1)(A), instructs the Commission

> to prescribe rules and regulations establishing reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such person, or in which such person has **an attributable interest**.[4]

Section 628(b) provides that:

> It shall be unlawful for a cable operator, a satellite cable programming vendor in which a cable operator has **an attributable interest** or a satellite broadcast programming vendor to engage in unfair methods of competition or unfair or deceptive acts or practices, the purpose or effect of which is to hinder significantly or to prevent any multichannel video programming distributor from providing satellite cable programming or satellite broadcast programming to subscribers or consumers.[5]

The attribution rules seek to identify those corporate, financial, partnership, ownership and other business relationships that confer on their holders a degree of ownership or other economic interest, or influence or control over an entity engaged in the provision of communications services such that the holders should be subject to the Commission's regulation.

3. Depending on the particular substantive rule and objective to be accomplished, a variety of different attribution standards are used in the Commission's rules. In the cable television area, there are, generally speaking, two strains of attribution rules: the "general attribution

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[4]47 U.S.C.§533(f)(1)(A) (emphasis added).

[5]47 U.S.C.§548(b) (emphasis added).

standard" and the so-called "program access attribution standard."[6] The general standard is based on, but not identical to, the broadcast attribution rules.[7] Under the general attribution standard, voting stock interests of 5% or more are attributab[8]] For passive institutional investors, voting stock interests of 10% or more are attributable.[9] Nonvoting stock interests, options, warrants and debt are not attributable[10] The general attribution standard provides a "single majority shareholder" exception to the voting stock threshold, which provides that a minority shareholder's voting interests will not be attributed where a single shareholder owns more than 50% of the outstanding voting stock.[11] Partnership interests and direct ownership interests are attributable regardless of the level of equity invested.[12] However, the interests of "insulated" limited partners are not attributed.[13] Directors and officers are also deemed to have an attributable interest.[14] The general attribution standard rules at issue in this proceeding are those that are used in conjunction with the cable horizontal ownership limits rule[15]

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[6]For a history of how the cable attribution rules developed, see *Cable Attribution Notice* at paras. 2-9.

[7]See *id.*

[8]47 C.F.R.§76.501 n.2 (a).

[9]47 C.F.R.§76.501 n.2 (c).

[10]47 C.F.R.§76.501 n.2 (f).

[11]47 C.F.R.§76.501 n.2 (b).

[12]47 C.F.R.§76.501 n.2 (a).

[13]47 C.F.R.§76.501 n.2 (a).

[14]47 C.F.R.§76.501 n.2 (h).

[15]47 C.F.R.§76.503.

and the vertical channel occupancy limits rule.[16] We applied the broadcast or general attribution standard to the horizontal limits and channel occupancy limits rules because they constitute broad structural rules designed to promote competition and diversity in the video-programming marketplace.[17]

4. The Commission adopted the program access attribution standard for cable rules that are designed not only to promote competition and diversity, but also to deter specific discriminatory or improper conduct.[18] The program access attribution standard captures more investment interests than the general attribution standard. Under the program access standard, the single majority shareholder and insulated limited partner exceptions do not apply. In addition, nonvoting stock and limited partnership equity interests of 5% or more are attributable.[19] The program access attribution standard rules at issue in this proceeding are used in conjunction with the following rules: program access,[20] carriage of an unaffiliated programmer,[21] SMATV/cable cross-ownership prohibition,[22] asset transfers between a cable operator and

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[16]47 C.F.R.§76.504.

[17] *Implementation of Sections 11 & 13 of Cable Television Consumer Protection and Competition Act of 1992 -- Horizontal and Vertical Ownership Limits, Second Report and Order*, MM Docket No. 92-264, 8 FCC Rcd 8565, 8568-69, 8577-8579, 8593-8596 (1993) ("*Horizontal Ownership Second Report and Order*").

[18]See *Cable Attribution Notice* at paras. 5-8 and orders cited therein for discussion on why the restrictive attribution standard was selected to apply to the substantive cable rules at issue in this proceeding.

[19] *Id.* at para. 5; see. e.g., 47 C.F.R.§76.501(d) n.5 (attribution rules for the cable/SMATV cross-ownership prohibition rule).

[20]47 C.F.R.§76.1001.

[21]47 C.F.R.§76.1300.

[22]47 C.F.R.§76.501(d).

an affiliate,[23] rate pass-throughs for the programming services of an affiliated programmer,[24] leased access[25] and open video systems.[26]

5. This *Report and Order* will also adopt final rules for the definition of the term "affiliate" for purposes of the local exchange carrier ("LEC") portion of the "effective competition" test,[27] and the cable-telco buy-out provisions enacted in the Telecommunications Act of 1996.[28] We asked for comment on the appropriate definition of an affiliate under these rules in the *Cable Reform Notice*.[29] However, because the *Cable Attribution Notice* initiated a more general review of the cable affiliation and attribution rules,[30] we decided to address these two issues in this proceeding.[31] We incorporate the Cable Reform comments into the record of this proceeding and rely on them in order to issue these final rules.[32]

6. Finally, we note that the *Broadcast Attribution* proceeding addressed the attribution rules that apply to the cable/broadcast station and ca-

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[23]47 C.F.R.§76.924(i).

[24]47 C.F.R.§76.922(f)(6).

[25]47 C.F.R.§76.970(b).

[26]47 C.F.R.§76.1503(c).

[27]See Communications Act§623(1)(1)(D), 47 U.S.C.§543(1)(1)(D).

[28]See Communications Act§652, 47 U.S.C.§572.

[29]*Cable Reform Notice*, 11 FCC Rcd 5937.

[30]See *Cable Attribution Notice* at para. 15 n.52 ("We seek comment on whether and how any changes in our cable attribution rules should affect our various definitions of 'affiliate.'").

[31]*See In re Implementation of Cable Act Reform Provisions of the Telecommunications Act of 1996, Report and Order*, CS Docket No. 96-85, FCC No. 99-57 at paras. 25, 91 (March 29, 1999) ("*Cable Reform Report and Order*").

[32]See Appendix B for a list of commenters in the *Cable Reform* proceeding.

ble/MMDS cross-ownership prohibitions; thus we do not address those rules in this *Report and Order*.[33]

B. Questions Raised in the *Cable Attribution Notice*

7. The *Cable Attribution Notice*, independently and through reference to the Broadcast Attribution Notice, sought comment on a number of issues relating to the attribution standards, including: (1) whether to increase the voting stock benchmark from 5 percent to 10 percent and the passive institutional investor benchmark from 10 percent to 20 percent; (2) whether to expand the category of passive investors; (3) whether and, if so, under what circumstances to attribute nonvoting shares; (4) whether to retain the single majority shareholder exemption from attribution; (5) whether to revise our insulation criteria for limited partners; (6) how to treat interests in limited liability companies ("LLCs") and other new business forms under the attribution rules; and (7) how to treat financial relationships and multiple business interrelationships that, although not individually attributable, should be treated as attributable interest when held in combination.

8. In addition to the issues raised in the initial *Broadcast Attribution Notice*, the *Broadcast Attribution Further Notice* explored additional proposals to increase the precision of the attribution rules. First, we invited comment on whether we should add a new equity/debt attribution rule. Under such a rule, where an interest holder is a program supplier or same-market media entity, we would attribute its otherwise non-attributable equity and/or debt interests in a media entity subject to the cross-ownership rules if those aggregated interests

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[33]This *Report and Order* nevertheless amends the attribution notes to 47 C.F.R.§76.501, which apply to the cable/broadcast station cross- ownership prohibition, because these notes are also used for our other cable rules. However, the amendments to these notes do not change the substance of the cable/broadcast attribution rules adopted in the *Broadcast Attribution Report and Order*.

exceed a specified benchmark, proposed to be set at 33 percent.[34] Second, we invited comments on a Commission staff study of attributable ownership interests in broadcast television stations, appended to the *Broadcast Attribution Further Notice*, and on the implications of this study regarding the impact of the proposed attribution rule changes, particularly as to the voting stock benchmarks.[35]

9. In addition to asking for comment on how these broadcast issues pertain to the cable industry, in the *Cable Attribution Notice* we asked for comment on (1) the proposed "equity plus debt" addition to the current cable attribution rules, and specifically those relationships in the cable context that may provide sufficient incentive and ability for an otherwise nonattributable interest holder to exert attributable influence or control; (2) the attribution of certain contractual or other business relationships in the cable context (including affiliations that allow different cable entities to purchase programming, technology or equipment on common terms) that may implicate diversity and competition concerns, irrespective of debt or equity; (3) the impact of raising the stock ownership benchmark for active and passive investors in the cable context, particularly seeking empirical data and analysis similar to the Commission staff study on the same subject in the broadcasting context; (4) whether to retain, modify, or eliminate the single majority shareholder exemption; and (5) whether a transition period or grandfathering of existing interests is appropriate if we decide to adopt more restrictive attribution rules.[36]

10. We also asked for comment on whether and how we should reevaluate the application of the program access attribution standard to certain of the rules described above, such as the program access and program carriage rules. Finally, we sought comment on whether and how any changes in our cable attribution rules should affect our

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[34] *Broadcast Attribution Further Notice* at paras. 8-25.

[35] *Id.* at paras. 36-38 and Commission staff study attached thereto.

[36] *Cable Attribution Notice* at para. 12.

various definitions of "affiliate."[37] In particular, we sought comment on whether and how those affiliation rules that are expressly based on our cable attribution rules should change if the underlying attribution rules are changed.[38] In the *Cable Attribution Notice*, we asked for comment on whether there were any relevant differences between the cable and broadcasting industries that would support a cable attribution standard that would differ from the broadcast attribution standard.[39] In this regard, we sought comment on any differences in, among other things, the ownership, financing or management structures of the cable industry and the broadcast industry that might warrant a different attribution standard.[40]

C. Summary of the Decisions of this Order

11. In general, we conclude that the cable industry's ownership and management structures do not in any relevant way differ from those of the broadcast industry such that the cable attribution rules should differ from the broadcast attribution rules. Thus, a large portion of this Report and Order will incorporate by reference the reasoning set forth in the *Broadcast Attribution Report and Order*. Where certain cable attribution rules depart from the broadcast attribution rules, the reasons for the departure are discussed. This *Report and Order* takes the following specific actions with regard to the cable attribution rules:

(1) retain the 5% voting stock attribution benchmark, but raise the passive institutional investor voting stock benchmark to 20%;

(2) retain the current definition of passive institutional investor;

(3) apply the limited partnership insulation criteria to limited

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[37] See, e.g., 47 C.F.R. ss 76.924(i), 76.970(b), 76.1500(g), 76.1401(b).

[38] *Cable Attribution Notice* at para. 15.

[39] *Cable Attribution Notice* at para. 13.

[40] *Id.*

liability companies;

(4) amend the insulation criteria for attribution of limited partnership interests for purposes of the horizontal ownership and channel occupancy limits rules;

(5) amend the waiver standard for the attribution of directors and officers for purposes of the horizontal ownership and channel occupancy limits rules;

(6) eliminate the single majority shareholder rule;

(7) adopt a 33% equity plus debt attribution rule that act as an exception to the insulated limited partner exception and the current exemptions from the attribution of non-voting equity and debt; and

(8) adopt certain transitional provisions relating to the application of these new rules to existing interests.

12. In addition, we clarify which entities are covered by the program access attribution standard. Under our substantive cable rules, such as the program access rule, it is arguable that the general attribution standard is applied to determine who or what constitutes a cable operator while the program access attribution standard is applied to determine who or what constitutes a programming vendor or other entity covered by the rule. Because the program access attribution standard was intended to apply to all entities under the rules where this standard applies, and because these substantive rules are designed to deter specific misconduct by all covered entities, we will amend these rules in order to clarify that the program access attribution standard applies to all entities covered by those rules. To reflect these clarifications of the attribution rules, we will amend our rules' various definitions of the term "affiliate" where appropriate.

13. With regard to the *Cable Reform* issues, we adopt the general cable attribution standard for the cable-telco buyout prohibition rule because that rule closely resembles the cable/SMATV cross-ownership rule, which is designed to promote competition. For the LEC affiliate prong of the effective competition test, we maintain the 10% voting equity benchmark proposed in the *Cable Reform Notice*, but devise a new

attribution rule for the LEC test.

14. Finally, we reject the cable operators' proposals that we discard the attribution rules in favor of an actual control approach to identifying cognizable interests. Such an approach would not accurately capture potentially influential or controlling interests, and would not be workable.

III. *Report and Order*

A. The General Attribution Standard

1. Background

15. In the *Cable Attribution Notice*, we requested comments relating to the general structure of the attribution rules; invited parties to discuss recent developments in the cable industry, including strategic alliances, partnerships, system swaps, mergers and acquisitions, relevant to application of these rules; and asked whether there were any differences in the ownership, financing or management structures, industry health, typical stockholdings, informal business arrangements, or outside financial claims of the cable industry and broadcast industry that would warrant different cable attribution rules.[41] This prompted a number of parties to suggest wholesale revisions to the traditional tools of the attribution rules. We address these comments first.

2. Comments

16. Cable operators generally, including NCTA, TCI,[42] and MediaOne,

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[41] *Cable Attribution Notice* at para. 16.

[42] On March 9, 1999, TCI merged with AT&T. TCI's cable systems are now owned by AT&T Broadband & Internet Services, Inc ("AT&T Broadband"), an AT&T subsidiary. TCI's programming subsidiary, Liberty Media Group, is now a separate subsidiary of AT&T. Because the comments in this proceeding were filed before the merger, we

argue that the cable horizontal ownership rules should not continue to follow the broadcast attribution rules because market conditions are different for the cable industry, new cable transactions allegedly insulate cable multiple system operators ("MSOs") from control over the newly created entities, and the Commission should adopt a "control" test for attribution. In response, alternative multichannel video programming distributors ("MVPDs") and a broadcaster argue that the market has not changed since the attribution rules were first enacted and that a "control" approach would not accurately capture influence and would not be workable.

a. Industry Differences

17. TCI argues that the Commission has in the past distinguished between different industries when it rejected a request that the broadcast attribution standard be applied to the telephone carrier/cable cross-ownership rule "largely because these two categories of multiple ownership rules relate at least in part to different industries, affect the interests of different parties, and have disparate underlying objectives."[43]

18. TCI notes that the purpose of the ownership rules is to promote competition and diversity. TCI contends that cable systems, unlike broadcasters, do not generally compete with each other in the same geographic areas for subscribers, local advertising revenues or programming.[44] As a result, TCI argues that the analysis of ownership concentration, competition, collusion and program diversity should

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will identify TCI's comments as those filed by TCI.

[43]TCI Comments at 8 n.15 (*quoting Reexamination of the Commission's Rules and Policies Regarding the Attribution of Ownership Interests in Broadcast, Cable Television and Newspaper Entities, Memorandum Opinion and Order*, MM Docket 83-46, 58 R.R.2d 604 at para. 22 (1985)).

[44]*Id.* at 12 n.26-27.

be different for cable than for broadcasting.[45] TCI, Comcast and NCTA argue that concerns regarding diversity are different for cable because, unlike a broadcaster, a cable operator provides dozens of channels to satisfy consumers.[46] Thus, NCTA argues that the ability of a minority interest in a cable system to significantly influence the viewing options available to a community cannot be equated with the magnitude of influence that a minority interest exerts on a single broadcast station that may only provide one programming option.[47]

19. MediaOne argues that the operators have not discouraged the development of new cable programming services.[48] By upgrading its systems from 550 MHz to 750 MHz, MediaOne states that it is adding 30 new analog channels, at least half of which will benefit unaffiliated programmers.[49] In addition, given the growth of direct broadcast satellite ("DBS") services, such as DIRECTV, which offers over 175 channels of cable programming, MediaOne states there is no longer reason for concern that operators will discourage new programming.[50] To compete with DBS, MediaOne states that operators must make diligent efforts to expand their channel capacity for new cable net-

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[45] *Id.* at 12 n.26-27.

[46] *Id.* at 15, NCTA Comments at 6; Comcast Reply Comments at 2.

[47] NCTA Comments at 6; *see also* Comcast Reply Comments at 5 (little risk that a minority, non-controlling investor will exert significant influence over the multitude of carried cable networks).

[48] MediaOne Comments at 6. Since 1992, cable networks have increased from 67 to 162, and of the 88 new networks, over 62% are unaffiliated with any cable MSOs. In addition, of the 77 newly planned cable networks, only 5 are affiliated with MSOs. *Id.* at 7 n.11 *(citing Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming, Fourth Annual Report,* 13 FCC Rcd 1034 Table F (1998) ("*1997 Competition Report*")).

[49] *Id.* at 10.

[50] *Id.* at 11; NCTA Comments at 6 (noting viewers can obtain alternative programming from other MVPDs).

works, regardless of an operator's interest in promoting affiliated programming.[51]

20. TCI argues that the evidence indicates that vertically integrated cable operators do not disfavor unaffiliated programmers in terms of rates or carriage.[52] In addition, TCI asserts that vertical mergers benefit consumers because a large, vertically integrated cable operator is better positioned than a stand-alone operator to know and satisfy consumers' viewing preferences.[53] Moreover, investors in cable operators are interested in the financial performance of the operator and will not, TCI asserts, tolerate actions designed to foreclose viewpoints or opinions for ideological purposes. Thus, widely held operators, TCI asserts, are prevented from controlling the viewpoints of the services they carry.[54]

21. Disputing the cable industry's arguments regarding the purposes of the applicable cable ownership rules, DIRECTV argues that the purpose of the various rules implicated in this proceeding is to check the bargaining power that MSOs have regarding programmers and the emerging MVPDs.[55] DIRECTV and Univision argue that the MSOs have not shown that the market has changed or that their behavior has changed, especially with regard to program access and must carry.[56]

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[51]MediaOne Comments at 11. TCI also argues that there are more programming outlets available today than when the big three networks were dominant. These include additional broadcast networks and non-cable MVPDs that provide service to more than 12 million homes. TCI Comments at 15-16.

[52]TCI Comments at 37.

[53]*Id.* at 39.

[54]*Id.* at 40.

[55]DIRECTV Reply Comments at 2-3; *see also* WCA Reply Comments at 3 (Commission should examine how liberalization of attribution rules will affect alternative MVPDs).

[56]DIRECTV Reply Comments at 2-3 (noting plethora of program access cases and the Commission's recent strengthening of the program access rules to provide damages);

DIRECTV notes that Comcast has refused to sell its Philadelphia regional sports network to DBS providers on the grounds that the program access rules do not apply to the terrestrial delivery of vertically integrated programming.[57] Univision states that regulatory safeguards such as must carry do not protect its cable network or its satellite-delivered network and that over half of its affiliated low-power stations are not entitled to must carry rights.[58]

b. The Cable Operators' Control Proposal

22. TCI and others, focusing on the horizontal ownership rules, argue that the current attribution standards impair the ability of cable operators to produce significant consumer benefits, realize efficiencies, and enhance competition in telephony and high speed data. Adelphia *et al.*, Time Warner, NCTA, TCI, Cablevision, MediaOne and Comcast propose various alternatives to the attribution rules where the investor would certify that it does not exercise control over the cable system at issue.[59] MediaOne, NCTA and TCI propose that minority interests not be attributable if the investor certifies that it does not control the

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Univision Reply Comments at 4 (noting that its San Francisco affiliate KDTV obtained on-channel cable carriage with 22 of TCI's 37 San Francisco systems only after the Commission ordered TCI to carry the affiliate in two 1998 orders); *see also* Univision Reply Comments at 8. Univision states that TCI dropped Univision's cable network in favor of TCI's affiliate, Telemundo, another Spanish-language network, once TCI acquired a Denver system. *Id.* at 9-10.

[57]DIRECTV Reply Comments at 5.

[58]Univision Reply Comments at 6.

[59]Adelphia *et al.* Comments at 3; Time Warner Comments at 34-35 ("a 5% equity interest is so small as to be essentially irrelevant"); Adelphia *et al.* Reply Comments at 3; Comcast Reply Comments at 3.

company's programming.[60] Regardless of the cable operator's interest or investment in a particular system, Adelphia *et al.* proposes that the Commission adopt a rule where a cable operator would be deemed to not "control" a system for horizontal ownership attribution purposes if it could certify that it (1) cannot dictate programming decisions, (2) does not control a majority of the governing board or committee, (3) does not prepare the operating or capital budget (but can review the budget prepared by the managing partner), (4) does not control personnel matters, (5) cannot dictate the use of particular technology, (6) does not have the unilateral right to acquire a controlling interest in the venture.[61] Adelphia *et al.* argues that a cable operator's super-majority approval rights over the sale of assets, dissolution or change of status of an entity are not indicia of control for attribution purposes.[62]

23. NCTA argues that unless an investor has control over a cable system, it is difficult to discern how diversity is implicated because there is little risk that a minority investor will restrict a company's editorial control.[63] TCI argues that an attribution standard based on operational control is the least restrictive and most efficient method for

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[60]MediaOne Comments at 25; MediaOne Reply Comments at 4; NCTA Comments at 10 (if an investor does not own 50% of more of a company's voting stock, the investor's interest should not be attributable if the investor certifies to the Commission that the investor cannot dictate programming decisions). TCI proposes that no interest, including a partnership interest, less than 10% be attributable. In cases where an MSO has an interest that is more than 10% and less than or equal to 50%, TCI argues that the interest should not be attributable if the MSO certifies that it will not control the company generally and specifically will not control the company with respect to programming, personnel, budget, and technological choices. TCI Comments at 2-3 n.3, 18-19.

[61]Adelphia *et al.* Comments at 20. Time Warner argues that a non-managing joint venture partner should be entitled to vote on budget matters without having an interest attributable to it. Time Warner Comments at 36.

[62]Adelphia *et al.* Comments at 12; *see also* Time Warner Comments at 35-37.

[63]NCTA Comments at 8.

the Commission to identify attributable interests. TCI states that attempting to identify "influential" interests in a set of rules is difficult given the alternative ways in which an interest holder's influence might be limited by factors which the rules do not examine.[64] TCI argues that a bright line test, such as the 5% equity interest benchmark, does not necessarily identify interests that posed a threat to the purpose of the ownership rules and therefore unnecessarily limits beneficial investments.[65] The cross-interest policy, which was adopted to identify influential interests not specifically addressed by the attribution rules, examined potential influential interests on a case-by-case basis. TCI argues that this ad hoc approach is slow and expensive.[66] TCI argues that the Commission permits regulated entities to self-certify in a variety of other circumstances because self-certification is efficient and less costly and does not impose an overbroad restriction or require a case-by-case determination.[67]

24. RCN argues that a "control" approach would not be workable because it is vague, would require the devotion of significant resources to a case-by-case analysis of each system, and would invite the creation of carefully designed corporate interests that would indicate lack of

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[64]TCI Comments at 26 (*citing An Economic Analysis of the Effects of Partial Ownership Interests in Cable Systems* at 8, Stanley M. Besen, Daniel P. O'Brien, John Woodbury, and Serge X. Moresi (Aug. 14, 1998) ("*Besen, O'Brien, Woodbury, and Moresi*") (attached to TCI Comments). For example, other large minority shareholders or a coalition of smaller shareholders might limit a minority shareholder's power. TCI Comments at 26; *Besen, O'Brien, Woodbury, and Moresi* at 8.

[65]TCI Comments at 28.

[66]TCI Comments at 30.

[67]TCI Comments at 20. For example, the Commission permits self- certification that a licensee does not cause unacceptable interference with the radio spectrum, an entity's passive investors are indeed passive, an applicant in a competitive bidding process is qualified to bid, an officer or director does not perform certain duties such that an interest should be attributed to the officer or director, and a limited partner's interest meets the insulation criteria. *Id.*

control on paper but would not reflect the actual influence that such interests would carry.[68] RCN observes that the practicalities of corporate decision-making are different from structures set forth on paper. RCN argues that a rational decision-maker will make decisions in the best interests of its investors, whether the investors vote or not.[69] CU states that cable operators need little or no direct ownership in a cable system in order to exert pressure with contractual rights.[70] CU states that partners who have minimal ownership use methods to protect their interests by creating options, put-sell provisions, and rights of refusal provisions in partnership agreements.[71]

25. NCTA asserts that the Commission has endeavored to "permit arrangements [under the attribution rules] in which a particular ownership or positional interest involves minimal risk of influence, in order to avoid unduly restricting the means by which investment capital may be made ...."[72] Most of the cable operators argue that the current rules interfere with the benefits of clustering their systems.[73] They argue that clustering benefits subscribers by enabling cable operators to lower costs; improve current services; more efficiently deploy new, innovative services such as internet, interactive video and telephony; develop and distribute regional programming services; and provide centralized, more responsive customer service.[74]

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[68]RCN Comments at 14-15.

[69]RCN Reply Comments at 16.

[70]CU Comments at 3.

[71] *Id.* at 3.

[72]NCTA Comments at 9 *(citing Review of the Commission's Regulations Governing Attribution of Broadcast Interests,* MM Docket No. 94-150, 10 FCC Rcd. 3606, 3610 (1995)).

[73]MediaOne Comments at 30; NCTA Comments at 23.

[74]Cablevision Comments at 10, 13 ("As the Commission has recognized, clustering can 'reduce costs and improve operating and management efficiencies,' position cable

26. AT&T, TCI, NCTA and MediaOne argue that the Commission should take into account not only the benefits to video programming, but also the benefits that clustering and economies of scale offer for bundled voice, data and cable services.[75] They argue that the Commission should consider the benefits of enabling cable operators to compete with incumbent local exchange carriers ("ILECs") to provide these services.[76] Cable operators argue that they cannot compete with ILECs without being able to form larger clusters comparable in size to the areas served by some of the newly merged ILECs, which are not subject

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operators to serve as an outlet for regional advertising, and 'enhance MSOs ability to compete successfully in the future with LECs and major electric utilities as providers of data transmission and local telephone services."') (*quoting 1997 Competition Report*, 13 FCC Rcd at 1115); Bresnan Comments at 6-7 (clustering systems lowers per-subscriber cost of new services because more people bear the cost); AT&T Comments at 11 (large customer base must be substantial to justify upgrading facilities to compete with ILECs); TCI Comments at 49-53; TCI Reply Comments at 19 (noting that a cable operator with a small subscriber base would not be able to recover its development costs for cable internet development); Bresnan Comments at 5, 22- 23 (cable modems and digital cable television); NCTA Comments at 9 (clustering reduces duplicative costs); MediaOne Comments at 14; Time Warner Comments at 10; Adelphia *et al.* Reply Comments at 6; Comcast Reply Comments at 6; Cablevision Reply Comments at 7. MediaOne also argues that clustering enables MSOs to advertise their services in order to counter competition from other types of MVPDs. MediaOne Comments at 14.

[75]MediaOne Comments at 7; AT&T Comments at 5 (noting that two of the horizontal limits statutory factors require the Commission to examine "any efficiencies and other benefits" of increased ownership and "the dynamic nature of the communications marketplace"); TCI Comments at 46-49; NCTA Comments at 12 (Commission should take note of convergence of technologies); MediaOne Reply Comments at 2 (current rules hinder its ability to deliver advanced services); Time Warner Reply Comments at 6. MediaOne states that by the end of 1998, over 2.4 million homes passed by its network will be able to receive high-speed Internet access service. MediaOne Comments at 17.

[76]AT&T Comments at 6-9; MediaOne Reply Comments at 9. NCTA and TCI note that an ILEC, Ameritech, opposes clustering. NCTA Reply Comments at 4; TCI Reply Comments at 15.

to subscriber limitations and are able to enjoy the benefits of economies of scale.[77]

27. Adelphia *et al.* argue that there are numerous benefits to their alliances with TCI: (1) TCI partners are able to create more efficient and larger regional clusters, (2) Falcon and Insight will be able to maintain a presence in the cable market unlike other independent cable operators who have been forced to sell, (3) TCI partners benefit from TCI's capital and technical experience, and (4) their alliances with TCI have enabled the partners to reach a critical mass so that they are able to offer better, less expensive technology to subscribers.[78] As a result of clustering and TCI's financial, technical and programming support,

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[77]Cablevision Comments at 3, 9-10 (arguing that clustering will enable cable operators to remain competitive with their rivals such as the newly merged Bell Atlantic/NYNEX/GTE and SBC/Pacific/Ameritech/SNET); Bresnan Comments at 6; Cablevision Reply Comments at 18-19; Comcast Reply Comments at 6; Time Warner Reply Comments at 8 (combined SBC/Ameritech and combined Bell Atlantic/GTE will respectively control 33.8% and 35.8% of the nation's local access telephone lines); AT&T Comments at 10; TCI Comments at 53-56; Time Warner Comments at 10; MediaOne Reply Comments at 9; NCTA Reply Comments at 4 (cable's potential as a competitive local exchange carrier is dependant on clustering); MediaOne notes that other cable competitors are also not limited to size limitations, such as DBS providers. *Id.* In MediaOne's largest region, the Northeast, it provides service to 1.2 million customers while the FCC-approved merger of Bell Atlantic and NYNEX provides 43,714,000 access lines. *Id.* at 18. MediaOne argues permitting clustering is the only affordable way to achieve these benefits and attract the capital that the LECs are capable of attracting. MediaOne Comments at 15. According to MediaOne, NYNEX saved more than 25% on a $1.5 billion purchase as a result of its merger with BellAtlantic, and SBC and Ameritech project $1 billion in annual savings from their planned merger. *Id.* at 18. The CLECs were able to raise $15 billion over two year to construct local exchange facilities, and five regional bell operating companies and GTE invested $24 billion in 1996 and $26.3 billion in 1997 to enhance their networks for advanced data services. *Id.* at 20; *see also* MediaOne Reply Comments at 9.

[78]Adelphia *et al.* Comments at 11-12. Falcon also states that it was not able to obtain capital for upgrading its systems until it entered into an alliance with TCI. *Id.* at 10. LCI states that it has been able to benefit from the research and experience that only a large MSO like TCI can afford. *Id.* at 19.

TCA and Bresnan argue that they are able to rebuild their systems to provide hybrid fiber coaxial ("HFC") architecture which enables them to provide more channel capacity, multiplexed networks, advanced pay-per-view programming, internet service and telephony.[79]

28. Cablevision acquired approximately 800,000 subscribers from TCI in the New York area, which brought Cablevision's number of subscribers to more than 2.5 million in the New York metropolitan area.[80] Cablevision argues that without TCI's involvement, Cablevision would not have been able to cluster its systems and develop an economy of scale that would have permitted it to achieve the economic benefits of clustering. Through clustering, Cablevision argues that it was able to successfully develop local programming because there are more local subscribers.[81]

29. DIRECTV and Ameritech argue that an MSO's subscribers do not pay lower costs simply because of the purported efficiencies of clustering. Rather, MSOs, they reason, are able to charge lower costs because they use their large size to obtain programming on more favorable terms than smaller companies: "Because this advantage is not grounded in superior efficiency, it is a barrier to effective competition in the multichannel video services industry."[82] TCI argues that if another cable operator cannot achieve the scale necessary to achieve lower

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[79]Bresnan *et al.* Comments at 7-12.

[80]Cablevision Comments at 4.

[81]Cablevision currently offers "MSG Metro" in the New York metropolitan area. MSG Metro consists of three channels that provide information and entertainment that reflect localized needs and interests. Cablevision Comments at 13 n.18. The ability to serve, as well as spread programming costs over, a greater number of subscribers in a geographically dense area increases the likelihood that a cable operator will develop local and regional programming. Bresnan Comments at 5.

[82]*J. Dertouzos & S. Wildman, Programming Access and Effective Competition in Cable Television* (Aug. 14, 1998) at i., attached to Comments of Ameritech. *See also* DIRECTV Reply Comments at 3-5; RCN Reply Comments at 9 (clustering gives MSOs ability to fight competition from emerging MVPDs).

programming costs, it should be attributed to that cable operator's unpopularity with consumers rather than the fact that another cable operator is able to obtain lower programming costs.[83]

30. RCN argues that how the MSOs will compete with LECs is irrelevant to this proceeding.[84] RCN and Univision argue that TCI's stake in Cablevision and its joint ventures with Adelphia *et al.* will give TCI an important voice in their business plans, harm consumers, and impede competition.[85] Ameritech argues that TCI's system swaps and joint ventures have significantly increased TCI's market power by giving it access to more subscribers.[86] For example, Ameritech notes that TCI's contribution of 850,000 subscribers to Cablevision now gives TCI an attributable interest in Cablevision's 3.5 million subscribers.[87] Given these joint ventures coupled with its ownership of Satellite Services, Inc. ("SSI") (a TCI subsidiary that sells to TCI partners "[m]any of the popular networks... at rates which are lower than those which would otherwise be obtainable"[88]), TCI can obtain, Ameritech asserts, virtually any terms it wants from a cable programmer, including exclusivity and steep discounts from even unaffiliated cable programmers.[89] Univision states that given TCI's investment in the joint ventures, it is implausible that the small cable operators will ignore any "suggestions" that TCI might make.[90] RCN notes that the FTC approval

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[83]TCI Comments at 8.

[84]RCN Reply Comments at 17.

[85]RCN Comments at 10, 14; RCN Reply Comments at 16; Univision Reply Comments at 13.

[86]Ameritech Comments at 8.

[87]*Id.* at 8.

[88]*Adelphia et al.* Comments at 8.

[89]*Id.* at 9.

[90]Univision Reply Comments at 13.

of the TCI/Cablevision transaction was based on an antitrust analysis, rather than the public interest analysis that the Commission should apply under Section 613 of the Communications Act, and is therefore irrelevant to this proceeding.[91]

31. Cablevision argues that its transaction with TCI enhances competition by enabling Cablevision to compete with Bell Atlantic, DIRECTV and RCN.[92] Furthermore, Cablevision argues that TCI's transactions actually reduce TCI's market power by transferring subscribers to another company.[93] Time Warner argues that the structure of TCI's joint ventures will not pose an anticompetitive risk.[94]

32. If the control certification proposals discussed above are not accepted or if an operator cannot make the necessary certification, Adelphia *et al.* argues that as long as the operator owns 50% or less of a venture and does not have managerial control, the operator should be attributed with only its pro rata share of the venture's subscribers.[95] Likewise, Time Warner and MediaOne propose that an MSO should only be attributed with the percentage of a corporation or a partnership's subscribers that equals the MSOs percentage equity interest in the corporation or partnership.[96] For example, if an MSO holds a 25% interest in a partnership, MediaOne argues that only 25% of the partnership's subscribers should be attributed to the MSO.[97]

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[91]RCN Reply Comments at 9.

[92]Cablevision Reply Comments at 9.

[93]*Id.* at 18.

[94]Time Warner Reply Comments at 27.

[95]Adelphia *et al.* Comments at 20-21; *see also* Bresnan *et al.* Comments at 22 (at the very least, the Commission should attribute only the percentage of an operator's cable subscribers to an investor that equals the investor's equity interest in the entity).

[96]Time Warner Comments at 18; MediaOne Comments at 26-28.

[97]MediaOne Comments at 26-28.

3. Discussion

33. The cable operators focus their arguments on the attribution rules applicable to the horizontal ownership rules. However, the cable operators have not presented a valid basis for a radical departure from our attribution rules framework, a framework that Congress found appropriate for the Commission to consider for the horizontal ownership rules.[98] The cable operators have not shown differences in the ownership, financing or management structures between the cable and broadcast industries that would warrant creating such a different type of attribution standard for the cable horizontal ownership or other cable rules.

34. Cable operators argue that the programming market has evolved so that even large MSOs have a limited impact on programming, and the attribution rules associated with the horizontal ownership rules inhibit cable clustering. In addition, they argue that the cable attribution rules should be different from the broadcast attribution rules because, unlike broadcasters, cable operators generally do not compete on the local level and the purposes of the broadcast and cable rules are different. These arguments are more appropriately addressed to the scope of the horizontal ownership rule itself, rather than the attribution rules. As we recently stated in the *Broadcast Attribution Report and Order,*

The attribution rules are designed to attribute entities that wield significant influence on core operations of the licensee. It is the ownership rules that limit investment based on our core policies of diversity and competition.[99]

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[98] *See Report of the Senate Committee on Commerce, Science and Transportation,* S. Rep. No. 92, 102d Cong., 1st Sess. 80 (1991) ("*Senate Report*") ("In determining what is an attributable interest, it is the intent of the Committee that the FCC use the attribution criteria set forth in 47 C.F.R.§73.3555 (notes) [the broadcast attribution rules] or other criteria the FCC may deem appropriate.").

[99] *Broadcast Attribution Report and Order* at para. 46.

Arguments with respect to the status of the programming market, vertical integration, non-cable competitors and cable clustering were properly raised and resolved in our companion Horizontal Ownership Third Report and Order.[100] Any changes to the horizontal ownership limits should be accomplished directly through an alteration of the limit rather than through a manipulation of what is considered to be ownership.[101]

35. In any event, we disagree with NCTA and TCI's argument that differences in the services that cable operators and broadcasters provide in the local market present a basis for establishing different sets of attribution standards for the local broadcast ownership rules and the cable horizontal ownership rules. What is relevant here is the market to which the rules are directed and the purposes of the rules. The appropriate market for an analysis of the horizontal ownership rules is the national market, not the local market.[102] In the horizontal ownership limits statute, Section 613, Congress directed the Commission to set limits on the concentration of ownership at the national level.[103] Congress was concerned that the anticompetitive effects of increased concentration at the national level might reduce the availability of diverse programming content.[104] Thus, although the local broadcast

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[100] *See Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992, Third Report and Order*, MM Docket No. 92-264, FCC No. 99-289 (Oct. 20, 1999) ("*Horizontal Ownership Third Report and Order*").

[101] *Broadcast Attribution Report and Order* at para. 46.

[102] *See Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming, Fifth Annual Report* at paras. 125, 152-153, CS Docket No. 98-102 (rel. Dec. 23, 1998) ("*1998 Competition Report*").

[103] See 47 U.S.C.§533(f)(1)(A).

[104] See 47 U.S.C.§533(f)((2)(A)-(G) for list of statutory factors that the statute directs the Commission to consider in order to preserving diverse and innovative programming. See *Horizontal Ownership Second Report and Order*, 8 FCC Rcd at 8568 ("Congress sought to prevent large, vertically integrated cable systems from creating barriers to entry for

rules and the horizontal ownership rules address different markets, their purposes are the same: both sets of rules are designed to promote competition within the industry and a diversity of viewpoints and programming.[105] Given that the cable horizontal ownership limits and the broadcast ownership rules serve similar purposes, it is appropriate, with certain exceptions discussed below, to use the same attribution standards for these rules. As discussed below, the cable operators do not persuade us that the broadcast attribution standards do not accurately capture equity or debt interests that convey influence or control.

36. We also continue to believe that the cable operators' "control" proposals, which we previously rejected in the *Horizontal Ownership Second Report and Order*,[106] do not take into account the variety of ways that an investor may exert influence or control over a company. An individual or firm does not need actual operational control over (or to be the management of) a company in order to exert influence and control over that company.[107] As discussed below, equity, debt and partnership interests confer on their holders influence and control, regardless of whether the holders maintain operational control of the company.[108] Moreover, the TCI transactions discussed in the record of

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new programmers and from causing a reduction in the number of media voices available to consumers.").

[105]See *Cable Attribution Notice* at para. 4.

[106]*Horizontal Ownership Second Report and Order* at para. 35.

[107]*See In re Amendment of Parts 20 and 24 of the Commission's Rules: Broadband PCS Competitive Bidding and Commercial Mobile Radio Service Spectrum Cap, Report and Order,* WT Docket No. 98-205, FCC 99-244 at para. 91 (Sept. 22, 1999) (rejecting control proposal for wireless rules).

[108]*See In re Amendment of Parts 20 and 24 of the Commission's Rules: Broadband PCS Competitive Bidding and Commercial Mobile Radio Service Spectrum Cap, Amendment of the Commission's Cellular/PCS Cross-Ownership Rule, Report and Order* WT Docket No. 96-59, GN Docket No. 90-314, FCC 96-278, 11 FCC Rcd 7824 at para. 121 (1996) (rejecting control proposal by noting that minority owner may exert influence by challenging

this proceeding demonstrate the control proposal's lack of credibility.[109] TCI's transactions include joint ventures where it has between a third and half the members of the board, rights of first refusal and supermajority rights or the right to veto fundamental decisions such as the sale of assets, declaration of bankruptcy, issuance of equity interests, consolidations, mergers, and capital calls. These rights clearly confer some degree of control or influence by TCI over the joint ventures. We agree with RCN and CU that, under these circumstances, it is more likely that a reasonable entity will consider the spoken or unspoken interests of its investors.

37. TCI's relationships with its partners demonstrates the influence that an investor can have over an entity even if the investor does not have actual, operational control over the entity's programming. Each of TCI's partners may take advantage of TCI's industry alliances, even if the partner is not required by TCI to do so. In the case of programming, each of TCI's partners can purchase at a low price cable programming networks that TCI has chosen to do business with.[110] We find it unlikely that the TCI partners would purchase the same cable networks at a higher price from a company other than TCI's subsidiary, SSI. We agree with Ameritech that the programming purchases by TCI's partners from SSI extend TCI's power in the programming marketplace.[111] Cable networks selected for carriage by TCI have a greater chance of being carried by the TCI partners. Conversely, cable networks not carried by TCI are placed at a disadvantage because they are

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business decisions, conducting or threatening litigation or by insisting upon business audits).

[109]See Attachment C for details of MSO transactions.

[110]See Adelphia *et al.* Comments at 8-9; Bresnan *et al.* Comments at 13.

[111]Given these joint ventures coupled with its ownership of SSI, TCI can obtain, Ameritech asserts, virtually any terms it wants from a cable programmer, including exclusivity and steep discounts from even unaffiliated cable programmers. Ameritech Comments at 8.

required to compete with discounted SSI cable networks for carriage on the TCI partners' cable systems.

38. In addition, the control proposals would be unworkable and would not provide regulatory certainty.[112] Under the control proposals, there are too many variables that the Commission and interested parties would have to weigh before a determination of non-con... could be made. For example, the Commission would be required to examine, among other things, the contracts between the parties (such as contracts between TCI's programming distributor subsidiary SSI and the TCI affiliates), the entity's corporate documents, the prior and current course of dealings between the parties, the structure of their board and management, and the rights and obligations of the interested parties. Many of these factors are subject to change over time.

39. With regard to the proposal that an investor be apportioned a percentage of a cable system's subscribers equal to the investor's percentage equity interest, we find no basis in the statute or in fact or theory to support such a rule. This proposal assumes that there is some logical basis for attributing an investor only some proportional influence over a cable system commensurate with the investor's percentage equity interest or that there would be some equitable reason to proceed in this manner. Investor A's 25% equity interest in cable system X, however, does not limit investor A's influence to 25% of cable system X's subscribers or 25% of the decision made by the system. Investor A's 25% equity interest enables it to exert influence or control over all aspects of the operation of the system, including what programming the system selects for all of its subscribers

B. Voting Equity Benchmark

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[112] *See In re Amendment of Parts 20 and 24 of the Commission's Rules: Broadband PCS Competitive Bidding and Commercial Mobile Radio Service Spectrum Cap, Report and Order*, WT Docket No. 98-205, FCC 99-244 at para. 91 (Sept. 22, 1999) (rejecting control proposal for wireless rules).

40. We turn next to suggestions for more specific changes in the attribution rules and address first those provisions of the rules that apply in common to both the general and program access attribution provisions. For both types of rules a 5% voting equity interest would be considered an attributable interest.[113] A number of parties have suggested that 5% is too low a number.

1. Comments

41. Bresnan, Time Warner, Chase, Mediacom and Comcast argue that the attribution standard for the cable horizontal ownership cap should be relaxed so that cable operators will have greater access to capital in order to upgrade their systems to true broadband service,[114] to implement new technologies, such as digital television,[115] and to increase investment in new programming services.[116] Bresnan argues that TCI's ownership interest in it and TCI's assistance to it will benefit subscribers who will then have access to hundreds of channels of programming at low costs due to the cost efficiencies of Bresnan's partnership with TCI.[117] Chase argues that the 5% voting interest threshold is simply too low a threshold for many institutions to invest.[118] Chase reasons that

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[113]47 C.F.R.§501 n. 2(a).

[114]Bresnan Comments at 15-16; Time Warner Comments at 46; Comcast Reply Comments at 3-4; Time Warner Reply Comments at 23-25; Chase Comments at 3; Mediacom Comments at 2-6. MediaOne states that cable operators will spend between $20 and $28 billion to upgrade their systems to accommodate internet, telephony, and digital programming. MediaOne Comments at 7-8; *see also* NCTA Comments at 14.

[115]Time Warner Comments at 47-49

[116]Time Warner Comments at 49.

[117]Bresnan Comments at 17-18.

[118]Chase Comments at 4. Chase is an institutional investor that holds an attributable interest (less than 10%) in Mediacom, a cable systems operator, and a 23% interest in

raising the voting benchmark to 10% will not give investors ultimate control over the company, but will recognize that investors must have some input to reduce the risk of the investment.[119]

42. Except for the horizontal ownership attribution rules that Time Warner believes should be abolished, Time Warner argues that the Commission should raise the voting benchmark to at least 10% and could safely raise it to 20% in order to increase the availability of capital.[120] NCTA argues that there has been no showing that an investor with a 5% interest has the ability to direct a system's core functions. NCTA notes that the Department of Interior uses a 10% threshold for acreage limitations, the SEC uses a 10% threshold for insider trading rules, and the Department of Transportation uses a 10% threshold for certain reporting requirements. Time Warner states that the Commission uses higher benchmarks for other rules such as a 20% direct and 25% indirect equity interest held by aliens in broadcast properties and the 40% interest that small businesses or rural telephone companies are permitted to hold for purposes of the CMRS spectrum aggregation limit.[121]

Wireless One, Inc. ("Wireless One"), a wireless cable service provider. Because Wireless One provides wireless services in some franchise areas served by Mediacom and because Chase's interest in both entities are currently attributable under the cable/MDS cross ownership restriction, Mediacom applied for and attained a twelve month waiver of the restriction. Mediacom Comments at 1-2. Chase and Mediacom also request that the Commission relax the more restrictive attribution standard applicable to the cable/MMDS cross-ownership rule. Chase Comments at 7-8; Mediacom Comments at 11-16. This issue was not raised in the *Cable Attribution Notice* and was in fact resolved in the *Broadcast Attribution Report and Order.*

[119]Chase Comments at 5.

[120]Time Warner Comments at 51-52 (Time Warner argues that Seagram Company Limited's 14.9% interest in Time Warner was not sufficient to dissuade Time Warner management from purchasing WTBS(TV)); *see also* Cablevision Reply Comments at 15 (recommending raising benchmark to 10%); Comcast Reply Comments at 3 (same).

[121]Time Warner Comments at 52-53.

43. TCI challenges the voting equity benchmark bright line test on the grounds that the "size of the financial interest [is] a highly imprecise indicator of the extent to which the financial interest conveys control."[122] TCI asserts that, in order to determine an investor's control, other factors must be examined, such as the composition of the board, who has authority over management, and the size of other minority shareholders.[123] However, TCI also argues that a case by case analysis of such factors would be too costly in terms of time and money.[124] TCI therefore proposes that the Commission adopt its control certification approach as a middle ground between a bright line test and a case by case analysis.

44. RCN argues that the program access standard should apply to the horizontal ownership rules in order to prevent cable companies from clustering in major markets and blocking RCN from those markets.[125] Comcast states that RCN's request is based on little more than a desire to achieve a competitive advantage.[126] Time Warner states that the need for investment far outweighs a theoretical risk of anticompetitive influence and that RCN's proposal runs counter to the deregulatory intent of the Telecommunications Act of 1996.[127] Because RCN's clustering proposal is more appropriately addressed in the context of the substantive horizontal ownership rules, we do not address it here.[128]

2. Discussion

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[122]TCI Comments at 27 (*quoting Besen, O'Brien, Woodbury, and Moresi* at 8).

[123]TCI Comments at 27 (*citing Besen, O'Brien, Woodbury, and Moresi* at 8).

[124]TCI Comments at 30.

[125]RCN Comments at 16-17.

[126]Comcast Reply Comments at 8.

[127]Time Warner Reply Comments at 26.

[128] *See Horizontal Ownership Third Report and Order* at para. 62.

45. In establishing voting equity provisions of the attribution rules, we focus on issues of control or influence. The attribution rules are intended to exempt from attribution ownership or positional interests that present minimal risk of influence in order to avoid unduly restricting access to capital but to attribute those interests that permit a significant potential for influence or control.[129] Based on the record of this proceeding, our parallel review of the broadcast attribution rules, a review of similar standards by other regulatory agencies, and academic studies relating to corporate governance, we conclude that the existing 5% voting share benchmark better takes into account the relevant considerations than any alternative at has been proposed.[130] We recognize that the dynamics of corporate life are varied and change over time. Thus, it is understandable that a provision of this type may be thought to be an ill fitting test of control or influence in some circumstances that might be revealed by a detailed review of the facts of particular situations. Such a particularized review process, however, would provide no certainty to parties planning transactions and would not necessarily lead to enduring conclusions even as to a particular entity. It is necessary therefore to analyze general benchmarks in order to develop a proper standard.

46. In earlier proceedings, we found, based on an ownership survey, that, in a widely-held corporation, a 5% shareholder is likely to be one of the largest 2 or 3 shareholders and therefore to be in a position to command the attention of management, and that a 5% benchmark was an appropriate threshold for attribution of interests in a closely-held corporation based on several possible ownership scenarios.[131] There is a body of more recent academic evidence that tends to confirm our

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[129]Broadcast Attribution Notice, 10 FCC Rcd at 3610.

[130]See *Broadcast Attribution Report and Order* at paras. 10-15.

[131]*Attribution of Ownership Interests*, 97 FCC 2d 997, 1005-08 (1984) ("*Attribution Order*"); *on recon.*, 58 RR 2d 604 (1985) ("*Attribution Reconsideration*"), *on further recon.*, 1 FCC Rcd 802 (1986) ("*Attribution Further Reconsideration*").

earlier conclusions, demonstrating that interest holders of 5% can likely exert considerable influence on a company's management and operational decisions. One recent study demonstrated that block trades involving 5 to 10 percent of a firm's voting stock resulted in a 27 percent turnover rate of the chief executive officer of the traded firm, that a 20 to 35 percent block trade resulted in a 40 percent turnover rate of the CEO, and that block trades over 35 percent of the voting equity resulted in a 56 percent turnover rate.[132] The turnover of the CEO was tracked over a one- year period following the date of the trade. These results, spanning an increasing level of ownership starting at 5 percent, demonstrate a consistent relationship between ownership trades and the rate of replacement of top management. The results imply that investors who acquire and hold such large blocks of voting stock can influence the choice of management of the firms in which they invest.

47. Another study presents evidence that 5 percent or greater stockholders vote more actively than less-than-five percent shareholders, and they tend to vote more often against the recommendations of management in votes over corporate anti-takeover amendments.[133] This study suggests that larger owners, starting at a 5 percent level of ownership, tend to be more active in influencing management than smaller owners. The two studies considered together provide evidence that ownership percentages starting at 5 percent can influence management policies.

48. Based on these studies, we therefore disagree with TCI's argument that the voting equity benchmark is too highly imprecise to be usable in the rules. Moreover, the voting equity benchmark is superior to a test requiring a case- by-case review of each and every cable transaction because it reduces regulatory costs, provides regulatory certainty, and permits planning of financial transactions.

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[132]L.E. Ribstein, *Business Associations* 987 (1990).

[133]J.A. Brickley, R.C. Lease and C.W. Smith, *Ownership Structure and Voting on Anti-takeover Amendments*, 20 Journal of Financial Economics 267-291 (1988).

49. We also disagree with commenters' arguments that the cable equity benchmark should conform to certain 10% benchmarks adopted by other federal agencies.[134] Those agencies' rules serve different interests than the Commission's ownership rules. For example, the Department of Transportation's 10% rule is designed to identify substantial interests, and the SEC's insider trading rule is designed to prevent intrinsically illegal or undesirable activities. Our rule is more analogous to the SEC's 5% ownership reporting benchmark.[135] Under the SEC 5% benchmark, any person who becomes a direct or indirect owner of more than 5% of any class of stock of a company must file a statement with the SEC.[136] The general purpose of this reporting requirement is to ensure that investors are alerted to potential changes in control, which is similar to the attribution rule's goal of identifying interests which confer on their holders the potential for influence or control.[137]

50. The commenters in this proceeding have not shown that other Commission attribution rules have similar purposes to the cable rules such that the attribution standards should be the same. The 40% CMRS spectrum rule[138] is designed to foster ownership by certain entities that have traditionally had difficulty gaining access to capital.[139] Likewise, the commenters have not show how the alien ownership limits have

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[134]See *Broadcast Attribution Report and Order* at para. 15 n.35.

[135]See *id.*

[136]Section 13(d)(1) of the Exchange Act, 15 U.S.C.§78m(d)(1).

[137] *See Securities and Exchange Commission v. Savoy Industries, Inc.*, 587 F.2d 1149 (1978), cert. denied, 99 S.Ct. 1227 (1979).

[138]47 C.F.R.§20.6(d)(2).

[139] *Broadcast Attribution Notice*, 10 FCC Rcd at 3623 n.68.

objectives similar to the rules involved in this proceeding.[140]

51. Regarding access to capital, we note that total capital available for cable investment is projected to double in 1999 at $ 24.160 billion from $12.326 billion in 1992.[141] Available capital has steadily grown from $16,731 billion in 1996, $21.396 billion in 1997 and $22.607 billion in 1998. In addition, in 1999, cable operators are projected to have approximately $3.44 billion in surplus capital available.[142] This dramatic increase in cable capital and capital surpluses decreases any cause for concern regarding the availability of capital.[143] Nevertheless, to the extent there remain any capital concerns, as discussed below, we are raising the passive investor benchmark to 20%.

C. Passive Institutional Investor Benchmark

1. Background

52. Our attribution rules do not attribute voting stock interests held by "passive investors" of less than 10%.[144] Passive investors are "investment companies, as defined by 15 U.S.C.§80a-3, insurance companies and banks holding stock through their trust departments in trust

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[140]We also note that the alien ownership restrictions of Section 310(b) of the Communications Act, as amended, apply only to "broadcast or common carrier or aeronautical en route or aeronautical fixed radio station" licenses. 47 U.S.C.§310(b).

[141]Paul Kagan Associates, Inc., Cable TV Finance at 2 (May 28, 1999) (noting that the cable industry is "celebrating two years of financial nirvana").

[142]*Id.*

[143]*See also Broadcast Attribution Report and Order* at para. 14 (finding that the strength of the communications and financial markets alleviated concerns over capital availability).

[144]See 47 C.F.R.§501 Note 2(c).

accounts."[145] In the Attribution Order, we concluded that these entities play passive roles because they lack the interest and the ability to actively participate in the firms in which they invest, and that setting a higher investment benchmark for such investors posed little risk of influence or control[146]

2. Comments

53. Some commenters request that the passive ownership benchmark be raised and the definition of passive investor be expanded. To increase capital availability, Time Warner argues that the threshold should be raised to 20%,[147] and TCI argues that it should be raised to 49%.[148] NCTA argues that the Commission should relax the passive ownership benchmark because passive investors by definition are not involved in a system's core functions and raising the benchmark will increase the flow of capital.[149] For small cable operators, NCTA argues that passive investments should not be attributable at all in order to give them more access to capital.[150]

54. Mediacom, Chase and Comcast argue that institutional investors should be treated as passive investors.[151] Chase argues that institutional investors invest in entities to obtain returns on their equity, not to harm the entities and diminish their profits; therefore, Chase argues that

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[145] *Id.*

[146] *Attribution Order* at para. 32.

[147] Time Warner Comments at 53.

[148] *Id.* at 51.

[149] NCTA Comments at 16; *see also* TCI Comments at 51 (passive investor safeguards will protect the public interest).

[150] NCTA Comments at 19.

[151] Mediacom Comments at 14-15; Comcast Comments at 3.

attribution standards for ownership rules should be distinguished from rules designed to control behavior, such as program access and program carriage.[152] Chase asserts that investment companies should be permitted to control seats of the board so long as they do not control the board and do not participate in the day-to-day operations of the entity in question.[153] Chase urges the Commission to recognize that investors must have some input to reduce the risk of the investment.[154]

3. Discussion

a. The Appropriate Passive Institutional Investor Benchmark

55. For the reasons set forth in the *Broadcast Attribution Report and Order*, we will raise the cable passive investor benchmark to 20%.[155] We believe that the legal and fiduciary requirements that constrain a passive institutional investor will ensure their passivity with respect to the management and operational affairs of a company. In addition, we believe that raising the benchmark is a relatively safe way to increase access to capital while continuing to capture influential interests. We will not raise the benchmark higher than 20%. As we stated in the *Broadcast Attribution Report and Order*, we must act cautiously when relaxing the attribution rules so that the purpose of the rules is not undermined. Based on the record before us in the Broadcast Attribution Proceeding, we found that voting stock held by passive investors could become decisive in proxy disputes, and passive investors accordingly could not be considered equivalent to limited partners

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[152]Chase Comments at 2 n.2, 3-5.

[153]Chase Comments at 8; *see also* Mediacom Comments at 9 (Chase is not actively involved in the management or operations of Mediacom).

[154]Chase Comments at 5.

[155]See *Broadcast Attribution Report and Order* at paras. 17-22. For the text of the new rule, see Appendix A; 47 C.F.R.§76.501.

or non- voting shareholders.[156]

b. Definition of Passive Investors

56. We will not expand the passive investor definition to include other types of investors. We are not convinced that other types of investors lack the interest or the ability to participate actively in companies in which they have invested.[157] This is particularly true of public pension funds, many of which have apparently become increasingly active in proxy fights and other devices to put pressure on management perceived to be under-performing.[158] Furthermore, commercial and investment bank activities do not fall under the same fiduciary restrictions, discussed above, that apply to bank trust departments. In addition, we have not been presented with sufficient evidence thus far to revise our earlier tentative conclusion not to include SBICs and SSBICs in the definition of passive investors.[159] As we have noted, under certain circumstances, these entities are authorized to exercise control over debtor companies for temporary periods.[160] Furthermore, an

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[156] *Id.* at para. 22.

[157] See *Broadcast Attribution Report and Order* at para. 25.

[158] M.J. Roe, *Strong Managers, Weak Owners* 125 (1994). In the *Attribution Order*, we declined to classify pension funds as passive investors based on evidence that pension funds manage their own investments and actively pursue social goals in their investment policies. *Attribution Order*, 97 FCC 2d at 1014-15.

[159] In the *Attribution Order*, we declined to accord passive status to SBICs and MESBICs, noting the absence of compelling reason to alter the 5 percent benchmark for these entities and the fact that while these entities are generally prohibited from assuming control of the companies in which they invest, they are authorized to exercise control over debtor companies for temporary periods under specified conditions. *Attribution Order*, 97 FCC 2d at 1016-17 & n. 45.

[160] Attribution Notice, 10 FCC Rcd at 3631, *citing Attribution Order*, 97 FCC 2d at 1016 & n. 45.

investment advisor, acting on behalf of its client, might exert the same level of influence or control as might the client. Therefore, unlike the categories currently defined as passive investors, we do not find evidence of regulatory or other safeguards ensuring that other types of investors will remain passive. While several commenters favored expanding the definition of the passive institutional investor category, they did not supply persuasive evidence or analysis to support their case and, in particular, to contradict evidence that these institutional investors can be actively involved in the companies in which they invest.[161] Indeed, the record here shows that some classes of institutional investors believe they should have the right to control seats on the board and to be actively involved.[162]

D. Partnership Interests

1. Comments

57. Under the Commission's current attribution rules governing partnership interests, general partners and non-insulated limited partnership interests are attributable, regardless of the amount or percentage of equity held. An exception from attribution applies only to those limited partners who meet the Commission's insulation criteria and certify that they are not materially involved in the management or operations of the partnership's media interests.[163]

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[161]Chase Comments at 5 (urging that investors must have some input in order to protect their investment).

[162]*Id.* at 5, 8.

[163]These "insulation criteria" include the following: (1) the limited partner cannot act as an employee of the partnership if his or her functions, directly or indirectly, relate to the media enterprises of the company; (2) the limited partner may not serve, in any material capacity, as an independent contractor or agent with respect to the partnership's media enterprises; (3) the limited partner may not communicate with the licensee or general partners on matters pertaining to the day-to-day operations of its business;

58. Time Warner argues that the attribution standards applicable to limited partnerships are overly restrictive in that a limited partnership investment no matter how small is attributable unless it is "insulated" under what Time Warner asserts are the Commission's overly-stringent standards.[164] Time Warner states that the Commission should change its insulation criteria to make them consistent with federal and state securities regulations which require that limited partners in "business development companies" be given the right to vote to elect or remove their general partners. In addition, Time Warner argues that the Commission should permit investors to communicate with the partnership about their investments and to enter into arms-length contractual relationships with respect to the partnership's business, as nonvoting or de minimus voting shareholders in corporations are permitted to do, without being attributable.[165] Finally, Time Warner argues that a limited partnership interest of less than 33% should not be attributable in any partnership with at least 20 limited partners if the partnership certifies that the interest holder will not be actively involved in the partnership's media affairs.[166]

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(4) the rights of the limited partner to vote on the admission of additional general partners must be subject to the power of the general partner to veto any such admissions; (5) the limited partner may not vote to remove a general partner except where the general partner is subject to bankruptcy proceedings, is adjudicated incompetent by a court of competent jurisdiction, or is removed for cause as determined by a neutral arbiter; (6) the limited partner may not perform any services for the partnership materially relating to its media activities, except that a limited partner may make loans to or act as a surety for the business; and (7) the limited partner may not become actively involved in the management or operation of the media businesses of the partnership. See *Attribution Reconsideration*, 58 RR2d at 618-20, on recon., 1 FCC Rcd at 802-03.

[164]Time Warner Comments at 55.

[165]*Id.* at 56-57 (giving a multiplicity of limited partners the right to remove a general partner does not give each limited partner significant influence or control).

[166]*Id.* at 57.

59. CU argues that the limited partner insulation exemption should be eliminated because, even though "insulated," limited partners nevertheless exercise some persuasion in partnership affairs that the attribution rules might not capture.[167]

60. Bresnan argues that the Commission should not eliminate its insulated limited partner exception because it would frustrate Bresnan's ability to upgrade its systems.[168] In addition, Bresnan argues that the Commission should apply its "single majority shareholder" exemption to partnerships because a minority shareholder does not have control, Bresnan asserts, over the entity.[169]

2. Discussion

61. For the reasons set forth in the *Broadcast Report and Order*, we find no basis to alter our conclusion that limited partnership interests are distinct from corporate equity voting interests and that our limited partnership insulation criteria are necessary to identify partnership interests that confer influence or control.[170] As we have previously found, partners in a limited partnership have the power, through contract, to determine their respective rights.[171] As a result, the power of a limited partner to influence or control the operations of the part-

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[167]CU Comments at 4.

[168]Bresnan Comments at 20.

[169]*Id.* Bresnan asserts that TCI's 20% general partnership interest in TCA II does not give TCI control over TCA II. Bresnan states that TCA II is governed by a partnership committee of five members, of which three are from TCA and two are from TCA. TCA has the explicit right to manage the day-to-day operations of the partnership and the right to purchase TCI's partnership interest, but TCI does not have the right to purchase TCA's interest. *Id.*

[170]*Broadcast Attribution Report and Order* at paras. 130-133; *see also* Attribution Further Reconsideration, 1 FCC Rcd at 803-04.

[171]*Id.*

nership may not be proportional to the limited partner's equity interest, because the extent of its power may be modified by contract.[172] Thus, the insulation criteria are designed to identify situations within which it is safe to presume that a limited partner will not be materially involved in the media management and operations of the partnership.[173]

62. We decline to loosen the insulation criteria to accommodate widely held limited partnerships, such as "business development companies," that are organized under federal and state laws that require that investors have powers to exert significant influence or control over their partnerships. Like partnerships, these new business entities have contractual flexibility for organizing their management, thereby giving their investors the contractual ability to determine their rights. More importantly, the federal and state laws that regulate business development companies and partnerships may permit and sometimes require those entities to organize themselves in a manner that would enable their members to exert significant influence or control over the partnership. Thus, federal and state laws may fail to provide sufficient assurances that a limited partner lacks the ability to be materially involved in the partnership's media activities, which is the central purpose of the insulation criteria. Accordingly, if an investor in a business development company cannot meet the insulation criteria because of a federal or state law, then the investor has the ability to significantly influence or control the company, which warrants attribution under our rules.[174]

63. Nevertheless, for the horizontal ownership and channel occupancy limits rules,[175] we agree with Time Warner that the insulation criteria

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[172] *Id.*

[173] *Id.*

[174] See *Broadcast Attribution Report and Order* at paras 131-132.

[175] 47 C.F.R. ss 76.503, 76.504.

should be revised. The horizontal ownership and channel occupancy limits are designed to address the ability of one MSO or a group of MSOs, by virtue of their size, to impede the flow of programming from the programmers to consumers.[176] An MSO may extend its ability to affect the programming marketplace when it invests in other cable companies. However, where the MSO is not materially involved in the video-programming activities of a limited partnership, its investment does not extend its national programming power and the concerns of Section 613 are not implicated. In these circumstances where programming is not affected, the current insulation criteria prevent investments between companies whose combination may bring benefits to the public, such as cable broadband and telephony services and competition to the incumbent local exchange carriers or Internet. In order for the limited partnership to benefit from an investor's expertise in these areas, it is necessary to craft insulation criteria that will not prevent the investor from offering its services to the partnership so long as those services are unrelated to the partnership's video-programming activities.

64. Therefore, we will amend the insulation criteria referenced in footnote 163 above for the horizontal and channel occupancy limits rules to provide that a limited partnership interest shall be attributed to a limited partner unless the partnership certifies that this limited partner is not materially involved, directly or indirectly, in the management or operation of the video- programming-related activities of the partnership.[177] In order to qualify for the insulated limited partnership exemption for purposes of these two rules, (1) the limited partner cannot act as an employee of the partnership if his or her functions, directly or indirectly, relate to the video-programming enterprises of the company; (2) the limited partner may not serve, in any material capacity, as an independent contractor or agent with respect to the

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[176]See 47 U.S.C.§613(f)(2)(A).

[177]See Appendix A, 47 C.F.R. ss 76.503, 76.504.

partnership's video-programming enterprises; (3) the limited partner may not communicate with the licensee or general partners on matters pertaining to the day-to-day operations of its video-programming business; (4) the rights of the limited partner to vote on the admission of additional general partners must be subject to the power of the general partner to veto any such admissions; (5) the limited partner may not vote to remove a general partner except where the general partner is subject to bankruptcy proceedings, is adjudicated incompetent by a court of competent jurisdiction, or is removed for cause as determined by a neutral arbiter; (6) the limited partner may not perform any services for the partnership materially relating to its video-programming activities, except that a limited partner may make loans to or act as a surety for the business; and (7) the limited partner may not become actively involved in the management or operation of the video-programming businesses of the partnership. Certifications pursuant to these rules should be served on the Commission as described in the notes to these rules.[178] In order for the Commission to accept the certification, the certification must be accompanied by facts, e.g. in the form of documents, affidavits or declarations, that demonstrate that the insulation criteria are satisfied.

E. Directors and Officers

1. Comments

65. Time Warner makes three requests for clarification of the attribution rules. First, according to Time Warner, alleged "dicta" in Mass Media decisions suggests that the power of a shareholder to appoint a corporate director is in itself an attributable interest.[179] Time Warner

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[178]See Appendix A, 47 C.F.R. ss 76.503, 76.504.

[179]Time Warner Comments at 64 (*citing Applications of Telemundo Group, Inc.*, 10 FCC Rcd 1104 at para. 24 n.8 (1994)).

requests that the Commission expressly disaffirm this type of attributable interest. Second, Time Warner argues that the Commission's recusal standard for the directors and officers of a parent company with regard to a subsidiary is imprecise and overbroad.[180] Third, Time Warner requests that the Commission clarify that, for purposes of Section 310(b) of the Communications Act, an alien entity may hold (1) noninsulated limited partnership interests in a broadcast licensee of up to 20% of equity or (2) indirect noninsulated limited partnership interests in a broadcast licensee of up to 25% of equity. Time Warner also requests that the Commission employ the multiplier to calculate the equity held indirectly by a noninsulated alien limited partner.[181]

2. Discussion

66. Directors and officers are deemed to have an attributable interest in the entities that they serve.[182] We disagree with Time Warner regarding the parameters of the directors and officers attribution rule. A party that has the right to appoint a director to the board of an entity has the ability to influence the entity's conduct by virtue of the director the party selects; thus under the directors and officers rule that party has an attributable interest in the entity.[183] Likewise, if two entities share common directors or officers, or have employees that serve as directors or officers of the other entity, the directors and officers render the entities attributable because of the influence that directors and officers have over an entity.

67. Time Warner argues that the recusal standard for the officers and directors of a parent company with regard to a subsidiary is imprecise

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[180] *Id.* at 65.

[181] *Id.* at 67.

[182] See 47 C.F.R.§76.503(h).

[183] See Telemundo Group, 10 FCC Rcd 1104 at para. 24 n.8

or overbroad.[184] As a general matter, we believe that the recusal standard is appropriate. In addition to the guidance provided by the rule, 47 C.F.R.§76.503(h) (officer or director's duties must be "wholly unrelated to the broadcast licensee or cable television system subsidiary"), the Commission has provided interpretative guidance in a series of decisions.[185] We have stated that parties must take steps to prevent "the recused director from exercising authority or influence in areas that will affect" the subsidiary.[186] For example, we have approved steps where the recused director is not involved in decisions or discussions regarding the particular subsidiary, financial reports are aggregated so that the subsidiary's performance figures are not separately displayed for the director, and reports to the director are redacted to remove information regarding the subsidiary.[187]

68. For purposes of the horizontal ownership and channel occupancy rules,[188] we will amend the matters for which a director or officer must recuse himself or herself in order to achieve the purpose of those rules. As discussed in Section III.D above, the horizontal ownership and channel occupancy rules are designed to place limits on a cable operator's programming power. As long as directors and officers appointed by a partial owner of a cable operator are not involved in the video-programming activities of the partially owned cable operator, the concerns of Section 613 that an MSO's programming power will be extended by its ownership interest are not implicated. Permitting

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[184] See 47 C.F.R.§76.503(h).

[185] *See, e.g., Telemundo Group*, 10 FCC Rcd at 1106; *Turner Broadcasting System, Inc.*, 11 FCC Rcd 19595 at para. 43 (1996); *Craig O. McCaw*, 9 FCC Rcd 5836, 5915-16 (1994), *aff'd sub nom., SBC Communications v. FCC*, 56 F.3d 1484 (D.C. Cir. 1995); *Viacom, Inc.*, 9 FCC Rcd 1577, 1579 (1994).

[186] *Turner Broadcasting*, 11 FCC Rcd 19595 at para. 20.

[187] *Telemundo Group*, 10 FCC Rcd at 1106.

[188] 47 C.F.R. ss 76.503, 76.504.

directors or officers who have knowledge and expertise in areas other than video programming, such as telephony or Internet, to serve with a cable company will benefit the cable company as technologies converge. Therefore, to achieve these objectives for the horizontal ownership and channel occupancy limits rules, appointed or common directors and officers, and the partnership equivalent thereof, shall not be attributable if they do not participate in the video programming activities of either entity.[189] To demonstrate that the officer or director meets the above-stated criteria, the relevant entity shall petition the Commission for a waiver as set forth in the rule.[190]

69. Finally, we will not address Time Warner's request regarding alien ownership of broadcast licensees. The *Cable Attribution Notice* did not raise for comment the attribution rules applicable to those rules; therefore, this is not the appropriate forum to address Time Warner's request.

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[189]See Appendix A, 47 C.F.R. ss 76.503, 76.504.

[190]See Appendix A, 47 C.F.R. ss 76.503, 76.504.

VI. Ordering Clauses

176. Accordingly, IT IS ORDERED, pursuant to Sections 4(i), 303 and 612, 613(f)(1)(A)&(B), 616, 623, 628 and 652 of the Communications Act of 1934, as amended, 47 U.S.C. ss 154(i), 303, 532, 533(f)(1)(A)&(B), 536(a), 543, 548(b), 572 and 573, that the amendments to discussed in this *Report and Order* and set forth in Attachment A ARE ADOPTED. These amendments shall become effective 70 days after publication in the Federal Register, following OMB approval, unless a notice is published in the Federal Register stating otherwise.

177. IT IS FURTHER ORDERED that the Commission's Office of Public Affairs, Reference Operations Division, SHALL SEND a copy of this Report and Order, including the Final Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration in accordance with paragraph 603(a) of the Regulatory Flexibility Act, Pub. L. No. 96-354, 94 Stat. 1164, 5 U.S.C.A.§601 et seq.

FEDERAL COMMUNICATIONS COMMISSION

Magalie Roman Salas
Secretary

Appendix A

Rule Changes

Part 76 of Title 47 of the Code of Federal Regulations is amended to read as follows:

PART 76 -- MULTICHANNEL VIDEO AND CABLE TELEVISION SERVICE

1. The authority citation for Part 76 continues to read as follows:

AUTHORITY: 47 U.S.C. 151, 152, 153, 154, 301, 302, 303, 303a, 307, 308, 309, 312, 315, 317, 325, 503, 521, 522, 531, 532, 533, 534, 535, 536, 537, 543, 544, 544a, 545, 548, 549, 552, 554, 556, 558, 560, 561, 571, 572, 573.

Section 76.501 Cross-Ownership

1. Section 76.501 is amended by revising Notes 1, 2, 5 and 6 as follows:

Note 1: Actual working control, in whatever manner exercised, shall be deemed a cognizable interest.

Note 2: In applying the provisions of this section, ownership and other interests in an entity or entities covered by this rule will be attributed to their holders and deemed cognizable pursuant to the following criteria:

(a) Except as otherwise provided herein, partnership and direct ownership interests and any voting stock interest amounting to 5% or more of the outstanding voting stock of a corporation will be cognizable;

(b) Investment companies, as defined in 15 U.S.C. 80a-3, insurance companies and banks holding stock through their trust departments in trust accounts will be considered to have a cognizable interest only if they hold 20% or more of the outstanding voting stock of a corporation, or if any of the officers or directors of the corporation are representatives of the investment company, insurance company or bank concerned. Holdings by a bank or insurance company will be aggre-

gated if the bank or insurance company has any right to determine how the stock will be voted. Holdings by investment companies will be aggregated if under common management.

(c) Attribution of ownership interests in an entity covered by this rule that are held indirectly by any party through one or more intervening corporations will be determined by successive multiplication of the ownership percentages for each link in the vertical ownership chain and application of the relevant attribution benchmark to the resulting product, except that wherever the ownership percentage for any link in the chain exceeds 50%, it shall not be included for purposes of this multiplication. [For example, if A owns 10% of company X, which owns 60% of company Y, which owns 25% of "Licensee," then X's interest in "Licensee" would be 25% (the same as Y's interest since X's interest in Y exceeds 50%), and A's interest in "Licensee" would be 2.5% (0.1 x 0.25). Under the 5% attribution benchmark, X's interest in "Licensee" would be cognizable, while A's interest would not be cognizable.]

(d) Voting stock interests held in trust shall be attributed to any person who holds or shares the power to vote such stock, to any person who has the sole power to sell such stock, and to any person who has the right to revoke the trust at will or to replace the trustee at will. If the trustee has a familial, personal or extra-trust business relationship to the grantor or the beneficiary, the grantor or beneficiary, as appropriate, will be attributed with the stock interests held in trust. An otherwise qualified trust will be ineffective to insulate the grantor or beneficiary from attribution with the trust's assets unless all voting stock interests held by the grantor or beneficiary in the relevant entity covered by this rule are subject to said trust.

(e) Subject to paragraph (i) of this Note, holders of non-voting stock shall not be attributed an interest in the issuing entity. Subject to paragraph (i) of this Note, holders of debt and instruments such as warrants, convertible debentures, options or other non-voting interests with rights of conversion to voting interests shall not be attributed unless and until conversion is effected.

(f)(1) Subject to paragraph (i) of this Note, a limited partnership interest shall be attributed to a limited partner unless that partner is not materially involved, directly or indirectly, in the management or operation of the media- related activities of the partnership and the relevant entity so certifies. An interest in a Limited Liability Company ("LLC") or Registered Limited Liability Partnership ("RLLP") shall be attributed to the interest holder unless that interest holder is not materially involved, directly or indirectly, in the management or operation of the media-related activities of the partnership and the relevant entity so certifies.

(2) In the case of a limited partnership, in order for an entity to make the certification set forth in paragraph (g)(1) of this section, it must verify that the partnership agreement or certificate of limited partnership, with respect to the particular limited partner exempt from attribution, establishes that the exempt limited partner has no material involvement, directly or indirectly, in the management or operation of the media activities of the partnership. In the case of an LLC or RLLP, in order for an entity to make the certification set forth in paragraph (g)(1) of this section, it must verify that the organizational document, with respect to the particular interest holder exempt from attribution, establishes that the exempt interest holder has no material involvement, directly or indirectly, in the management or operation of the media activities of the LLC or RLLP. The criteria which would assume adequate insulation for purposes of these certifications are described in the Memorandum Opinion and Order in MM Docket No. 83-46, FCC 85-252 (released June 24, 1985), as modified on reconsideration in the Memorandum Opinion and Order in MM Docket No. 83-46, FCC 86-410 (released November 28, 1986). Irrespective of the terms of the certificate of limited partnership or partnership agreement, or other organizational document in the case of an LLC or RLLP, however, no such certification shall be made if the individual or entity making the certification has actual knowledge of any material involvement of the limited partners, or other interest holders in the case of an LLC or RLLP, in the management or operation of the media businesses of the

partnership or LLC or RLLP.

(3) In the case of an LLC or RLLP, the entity seeking insulation shall certify, in addition, that the relevant state statute authorizing LLCs permits an LLC member to insulate itself as required by our criteria.

(g) Officers and directors of an entity covered by this rule are considered to have a cognizable interest in the entity with which they are so associated. If any such entity engages in businesses in addition to its primary media business, it may request the Commission to waive attribution for any officer or director whose duties and responsibilities are wholly unrelated to its primary business. The officers and directors of a parent company of a media entity, with an attributable interest in any such subsidiary entity, shall be deemed to have a cognizable interest in the subsidiary unless the duties and responsibilities of the officer or director involved are wholly unrelated to the media subsidiary, and a certification properly documenting this fact is submitted to the Commission. The officers and directors of a sister corporation of a media entity shall not be attributed with ownership of that entity by virtue of such status.

(h) Discrete ownership interests held by the same individual or entity will be aggregated in determining whether or not an interest is cognizable under this section. An individual or entity will be deemed to have a cognizable investment if:

(1) The sum of the interests held by or through "passive investors" is equal to or exceeds 20 percent; or

(2) The sum of the interests other than those held by or through "passive investors" is equal to or exceeds 5 percent; or

(3) The sum of the interests computed under paragraph (i)(1) of this section plus the sum of the interests computed under paragraph (i)(2) of this section is equal to or exceeds 20 percent.

(i) Notwithstanding paragraphs (e) and (f) of this Note, the holder of an equity or debt interest or interests in an entity covered by this rule shall have that interest attributed if the equity (including all stockholdings, whether voting or nonvoting, common or preferred, and partnership interests) and debt interest or interests, in the aggregate, exceed

33 percent of the total asset value (all equity plus all debt) of that entity, provided however that:

(1) in applying the provisions of paragraph (i) of this note to§76.501, §76.505 and§76.905(b)(2), the holder of an equity or debt interest or interests in a broadcast station, cable system, SMATV or multiple video distribution provider subject to§76.501,§76.505, or§76.905(b)(2) ("interest holder") shall have that interest attributed if the equity (including all stockholdings, whether voting or nonvoting, common or preferred, and partnership interests) and debt interest or interests, in the aggregate, exceed 33 percent of the total asset value (defined as the aggregate of all equity plus all debt) of that entity; and

(i) the interest holder also holds an interest in a broadcast station, cable system, SMATV, or multiple video distribution provider that operates in the same market, is subject to§76.501,§76.505, or§76.905(b)(2) and is attributable without reference to this paragraph (i); or

(ii) the interest holder supplies over fifteen percent of the total weekly broadcast programming hours of the station in which the interest is held.

(2) For purposes of applying subparagraph (i)(1), the term "market" will be defined as it is defined under the rule that is being applied.

Note 5: Certifications pursuant to this section and these notes shall be sent to the attention of the Cable Services Bureau, Federal Communications Commission, 445 12th Street, N.W. Washington, D.C. 20554.

Note 6: In applying paragraph (a) of§76.501, no minority voting stock interest will be cognizable if there is a single holder of more than 50% of the outstanding voting stock of the corporation in which the minority interest is held, provided however, that an investor that has an interest under the terms of Note 2(i) of this section shall have that interest attributed.

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Section 76.503 National subscriber limits

2. Section 76.503 is amended by adding Note 2 as follows:

Note 1: Attributable Interest shall be defined by reference to the criteria set forth in Notes 1-5 to§76.501 provided however, that:

(a) Notes 2(f) and 2(g) to§76.501 to shall not apply;

(b)(1) Subject to Note2(i) to§76.501, a limited partnership interest shall be attributed to a limited partner unless that partner is not materially involved, directly or indirectly, in the management or operation of the video programming-related activities of the partnership and the relevant entity so certifies. An interest in a Limited Liability Company ("LLC") or Registered Limited Liability Partnership ("RLLP") shall be attributed to the interest holder unless that interest holder is not materially involved, directly or indirectly, in the management or operation of the video programming-related activities of the partnership and the relevant entity so certifies.

(2) In the case of a limited partnership, in order for an entity to make the certification set forth in paragraph (b)(1) of this section, it must verify that the partnership agreement or certificate of limited partnership, with respect to the particular limited partner exempt from attribution, establishes that the exempt limited partner has no material involvement, directly or indirectly, in the management or operation of the video programming activities of the partnership. In the case of an LLC or RLLP, in order for an entity to make the certification set forth in paragraph (g)(1) of this section, it must verify that the organizational document, with respect to the particular interest holder exempt from attribution, establishes that the exempt interest holder has no material involvement, directly or indirectly, in the management or operation of the video programming activities of the LLC or RLLP. The criteria which would assume adequate insulation for purposes of these certifications are described in the *Report and Order*, FCC No. 99-288, CS Docket No. 98-82 (released October 20, 1999). In order for the Commission to accept the certification, the certification must be accompanied by facts, e.g. in the form of documents, affidavits or declarations, that demonstrate that these insulation criteria are met. Irrespective of the terms of the certificate of limited partnership or partnership

agreement, or other organizational document in the case of an LLC or RLLP, however, no such certification shall be made if the individual or entity making the certification has actual knowledge of any material involvement of the limited partners, or other interest holders in the case of an LLC or RLLP, in the management or operation of the video-programming activities of the partnership or LLC or RLLP.

(3) In the case of an LLC or RLLP, the entity seeking insulation shall certify, in addition, that the relevant state statute authorizing LLCs permits an LLC member to insulate itself as required by our criteria.

(c) Officers and directors of an entity covered by this rule are considered to have a cognizable interest in the entity with which they are so associated. If any such entity engages in activities other than video-programming activities, it may request the Commission to waive attribution for any officer or director whose duties and responsibilities are wholly unrelated to the entity's video-programming activities. In the case of common or appointed directors and officers, if common or appointed directors or officers have duties and responsibilities that are wholly unrelated to video-programming activities for both entities, the relevant entity may request the Commission to waive attribution of the director or officer. The officers and directors of a parent company of a video-programming business, with an attributable interest in any such subsidiary entity, shall be deemed to have a cognizable interest in the subsidiary unless the duties and responsibilities of the officer or director involved are wholly unrelated to the video-programming subsidiary, and a certification properly documenting this fact is submitted to the Commission. The officers and directors of a sister corporation of a cable system shall not be attributed with ownership of that entity by virtue of such status.

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Section 76.504 Limits on carriage of vertically integrated programming

3. Section 76.504 is amended by deleting paragraph (h) and adding Note 1 as follows:

Note 1: Attributable Interest shall be defined by reference to the criteria set forth in Notes 1-5 to§76.501 provided however, that:

(a) Notes 2(f) and 2(g) to§76.501 to shall not apply;

(b)(1) Subject to Note2(i) to§76.501, a limited partnership interest shall be attributed to a limited partner unless that partner is not materially involved, directly or indirectly, in the management or operation of the video programming-related activities of the partnership and the relevant entity so certifies. An interest in a Limited Liability Company ("LLC") or Registered Limited Liability Partnership ("RLLP") shall be attributed to the interest holder unless that interest holder is not materially involved, directly or indirectly, in the management or operation of the video programming-related activities of the partnership and the relevant entity so certifies.

(2) In the case of a limited partnership, in order for an entity to make the certification set forth in paragraph (b)(1) of this section, it must verify that the partnership agreement or certificate of limited partnership, with respect to the particular limited partner exempt from attribution, establishes that the exempt limited partner has no material involvement, directly or indirectly, in the management or operation of the video programming activities of the partnership. In the case of an LLC or RLLP, in order for an entity to make the certification set forth in paragraph (g)(1) of this section, it must verify that the organizational document, with respect to the particular interest holder exempt from attribution, establishes that the exempt interest holder has no material involvement, directly or indirectly, in the management or operation of the video programming activities of the LLC or RLLP. The criteria which would assume adequate insulation for purposes of these certifications are described in the *Report and Order*, FCC No. 99-288, CS Docket No. 98-82 (released October 20, 1999). In order for the Commission to accept the certification, the certification must be accompanied by facts, e.g. in the form of documents, affidavits or declarations, that demonstrate that these insulation criteria are met. Irrespective of the terms of the certificate of limited partnership or partnership agreement, or other organizational document in the case of an LLC or

RLLP, however, no such certification shall be made if the individual or entity making the certification has actual knowledge of any material involvement of the limited partners, or other interest holders in the case of an LLC or RLLP, in the management or operation of the video-programming activities of the partnership or LLC or RLLP.

(3) In the case of an LLC or RLLP, the entity seeking insulation shall certify, in addition, that the relevant state statute authorizing LLCs permits an LLC member to insulate itself as required by our criteria.

(c) Officers and directors of an entity covered by this rule are considered to have a cognizable interest in the entity with which they are so associated. If any such entity engages in activities other than video-programming activities, it may request the Commission to waive attribution for any officer or director whose duties and responsibilities are wholly unrelated to the entity's video-programming activities. In the case of common or appointed directors and officers, if common or appointed directors or officers have duties and responsibilities that are wholly unrelated to video-programming activities for both entities, the relevant entity may request the Commission to waive attribution of the director or officer. The officers and directors of a parent company of a video-programming business, with an attributable interest in any such subsidiary entity, shall be deemed to have a cognizable interest in the subsidiary unless the duties and responsibilities of the officer or director involved are wholly unrelated to the video-programming subsidiary, and a certification properly documenting this fact is submitted to the Commission. The officers and directors of a sister corporation of a cable system shall not be attributed with ownership of that entity by virtue of such status.

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APPENDIX C

Cable Alliances and Partnerships

To assist with our analysis in this proceeding, we asked for comment on the specifics of recently concluded cable transactions, such as cable system partnerships, joint ventures, swaps, transfers, mergers and acquisitions, particularly those transactions announced or consummated in 1997 or thereafter.

For each transaction identified, we asked the commenters to note the percentage and nature (e.g., voting or non-voting, limited or general partnership, insulated or non-insulated, rights of conversion) of each entity's ownership interests; the number of officers, directors, and other key personnel appointed by each entity to a management committee, board or other governing body; and the portion of the equity or debt financing contributed by each entity. In addition, we asked for comment on any authority or power held by each entity to review, veto or otherwise influence the management or operation of the cable systems, including core areas such as budget, personnel, programming, technology and competitive practices.

We note that, since the comments in this proceeding were filed, many of the alliances discussed below have changed.

i. Comcast

Comcast agreed to loan $735,000,000 to Prime Communications, LLC, in exchange for a 10-year note which is convertible to a 90% equity interest in Prime once Prime rebuilds its Washington, D.C. area cable systems. Until the note is converted, Prime will manage and operate its systems.[396] Prime serves approximately 430,000 customers, which under our new ED rule will be attributable to Comcast.

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[396] *Comcast Corporation Enters Into Strategic Relationship with Prime Communications, Press Release* (Dec. 11, 1998).

ii. MediaOne's Partnership with Time Warner

MediaOne holds a 25.5% limited partnership interest in a partnership with Time Warner, Time Warner Entertainment Co., LP ("TWE"). Thus, under the Commission's attribution rules, TWE's 9.6 million subscribers are attributed to MediaOne. MediaOne states that adding TWE's 9.6 million subscribers to the 4.9 million subscribers that MediaOne alone serves raises MediaOne's total number of subscribers to 14.5 million, which is higher than Time Warner's 12 million subscribers.[397] MediaOne states that it cannot avail itself of the "insulated limited partner" exception because one of the key purposes of the partnership was to combine Time Warner and MediaOne's expertise in designing and testing Full Service Networks.[398] MediaOne asserts that it has not exercised any control over the selection of programming on the TWE systems.[399] According to MediaOne, it directly serves only 8% of the nation's cable subscribers, but because the TWE subscribers are attributed to MediaOne under the current rules, MediaOne cannot acquire more than another 2.6 million subscribers without violating the 30% horizontal ownership limits.[400]

iii. TCI's Joint Ventures, Affiliations and Investments[401]]

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[397]FN397. MediaOne Comments at 3. MediaOne's numbers here are not calculated according to the Commission's attribution rules.

[398]*Id.* at 4.

[399]*Id.* at 4.

[400]*Id.* at 5.

[401]On March 9, 1999, TCI merged with AT&T. TCI's cable systems are now owned by AT&T Broadband & Internet Services, Inc ("AT&T Broadband"), an AT&T subsidiary. TCI's programming subsidiary, Liberty Media Group, is now a separate subsidiary of AT&T. Because the comments in this proceeding were filed before the merger, for ease of reference, we will refer to AT&T Broadband as TCI.

As of January 20, 1999, TCI states that, based on our current attribution rules, its cable systems pass 38,757,000 homes.[402]] Based on 95.6 million total cable homes passed, TCI's systems pass 45% of the market. With the exception of its investment in Time Warner, TCI's joint ventures, affiliations and investments described below attribute those entities' subscribers to TCI.

Adelphia *et al.* and Bresnan *et al.* state that each of TCI's affiliates has the option to purchase cable networks from TCI's subsidiary, Satellite Services, Inc. ("SSI"), but is not required to do so.[403]3] SSI purchases the distribution rights for cable program networ[404]] It provides "[m]any of the popular cable networks ... at rates which are lower than those which would otherwise be obtainable."[405] A TCI partner can selectively choose cable networks from SSI's offerings and is free to separately contract for non-SSI services.[406]

a) Time Warner

TCI, through its subsidiary Liberty Media, holds a 10% equity interest in Time Warner.[407] Pursuant to a consent decree with the Federal Trade Commission ("FTC"), Liberty Media exchanged its shares of Time Warner common stock for a separate series of Time Warner common

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[402]Letter to Magalie Roman Salas, FCC Secretary, from Douglas G. Garrett, TCI Senior Regulatory Counsel (Dec. 30, 1998).

[403]Adelphia *et al.* Comments at 8-9; Bresnan *et al.* Comments at 13.

[404]Adelphia et. al Comments at 8.

[405]Adelphia et. al Comments at 8.

[406]*Id.*

[407]Tele-Communications, Inc. 1997 Stockholder Report, Liberty Media Group Assets, at 19.

stock with limited voting rights.[408] Thus, Liberty Media's 10% equity interest in Time Warner represents less than 1% of the voting power of Time Warner's outstanding common stock.[409]

b) Adelphia Partnership

TCI holds a 34.4% interest and Adelphia Communications Corp. holds a 65.6% interest in Parnassos, LP. The partnership serves approximately 465,000 subscribers and passes approximately 700,000 homes. Adelphia has three members and TCI has two members on the five-member Parnassos board. Unanimous consent of the board is required for fundamental decisions such as the purchase/sale of assets, issuance of equity interests, consolidation, mergers, and additional capital calls.[410]0] Adelphia manages the Parnassos partnership for a fee and states that it has managerial control over programming choices, personnel, marketing, and rebuilds. Parnassos purchases programming from SSI.[411]

c) Falcon and Insight Partnerships

TCI holds a 47% interest in Falcon Communications, LP (a partnership with Falcon Holding Group, Inc.) and a 50% interest in Insight Communications of Indiana LLC (a partnership with Insight Communications Co., LP). The Falcon partnership serves approximately 1 million subscribers, and the Insight Partnership serves approximately 320,000 subscribers. The Falcon partnership agreement and the Insight agreement give Falcon and Insight, respectively, the exclusive right to manage their joint ventures with TCI, while TCI retains super majority

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[408]Tele-Communications, Inc. Merger Proxy Statement, Form DEF 14-A (Jan. 8, 1999).

[409]*Id.*

[410]TCI Comments at 42-43; Adelphia *et al.* Comments at 15.

[411]TCI Comments at 42-45; Adelphia *et al.* Comments at 15.

rights to approve fundamental decisio[412]] Of the six- member Falcon Communications, LP, advisory committee, Falcon will have three members, TCI will have two members, and TCI and Falcon will jointly agree on a sixth memb[413] The Insight Communications of Indiana LLCs management committee will consist of three Insight members and two TCI members.[414]14]

d) Lenfest Communications, Inc.

TCI holds a 50% corporate voting equity interest in Lenfest Communications, Inc. ("LCI"). H.F. Lenfest ("Mr. Lenfest") and his three children from whom he holds proxies own and control the remaining 50% of LCI's stock. LCI serves approximately 1 million subscribers. Mr. Lenfest has the right to designate a majority of the board's directors until January 1, 2002, at which time the Lenfest family and TCI will have the right to appoint an equal number of directors to the board. Mr. Lenfest is LCI's president and CEO and is guaranteed these positions until January 1, 2002. LCI states that TCI has no management control according to an agreement with Mr. Lenfest.[415] If LCI shareholders decide to sell their shares, TCI has the right of first refusal.[416] LCI purchases a number of SSI channels, but has negotiated contracts with channels non-affiliated with SSI and has declined to carry cable networks affiliated with SSI due to LCI's insufficient channel capacity.[417]] Although LCI contracted to use TCI's HITS digital pro-

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[412] Adelphia *et al.* Comments at 12, 14.

[413] *Id.* at 12-13.

[414] *Id.* at 14.

[415] *Id.* at 18.

[416] *Id.* at 20.

[417] *Id.* at 18-19.

gramming service, LCI states that it was under no obligation to do so.[418]

e) Peak Cablevision

TCI holds a 66.7% interest in Peak Cablevision, LLP (a partnership with Fisher Communications, LLC). Peak Cablevision serves approximately 112,000 subscribers and passes approximately 179,000 homes. Fisher will manage the Peak partnership for a fee, the four-member board will consist of two TCI members and two Fisher members, and all decisions will be made by a majority vote, except for major decisions, including budgets, which require unanimous approval. TCI provides programming to the partnership through SSI. [419]

f) Intermedia Capital Partners VI LP

TCI and its president Leo Hindery have an undisclosed interest as limited partners in Intermedia Capital Partners VI, LP. [420] Intermedia Capital Management VI, LLC is the general partner and manages the partnership for a fee. Intermedia serves approximately 425,000 subscribers and passes approximately 646,000 homes. The partnership's advisory committee consists of three TCI members, three Intermedia members and three members from the Blackstone Group, a limited partner. The advisory committee and the limited partners are prohibited from taking part in the control, management or operation of the partnership.[421] TCI provides programming to the partnership through SSI. [422]

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[418] *Id.* at 19.

[419] TCI Comments at 46.

[420] *Id.*

[421] *Id.* at 47.

[422] *Id.*

g) Cablevision

Cablevision acquired approximately 800,000 subscribers from TCI in the New York area.[423] In exchange for the subscribers, Cablevision gave TCI a 33% equity interest in Cablevision, but because TCI has class A stock, which has 1/10 the voting power of class B stock, TCI's voting interest is 8.8%.[424] Cablevision's chairman Charles F. Dolan has control over 44.7% of the total voting power, and other Dolan family members hold 36.8% of the total voting power.[425] Cablevision argues that TCI's control is limited in three other ways. First, for class votes, TCI must vote its shares in direct proportion to the votes of non-TCI Class shareholders; thus Cablevision argues that TCI has no independent voting power. Currently there are only four class A directors out of the 15 directors serving on the board. Second, TCI is prohibited from joining a voting group or voting trust and from obtaining beneficial ownership of more than an additional 10% of class A shares. Third, while TCI is entitled to designate up to two class B seats on the board, voting restrictions prohibit it from designating additional directors. Because class B stockholders have the power to appoint 75% of the board, the Dolan family has the ability to appoint a majority of the board.[426] Cablevision states that TCI has no meaningful ability to exercise influence or control over Cablevision's key decisions.[427] Cablevision states that the Federal Trade Commission ("FTC") found that the TCI/Cablevision transaction was not anticompetitive after a review under the Hart-Scott-Rodino Act.[428] Cablevision serves approx-

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[423]Cablevision Comments at 4.

[424]*Id.* at 15.

[425]*Id.* at 15-16.

[426]*Id.* at 16.

[427]*Id.* at 14, 17.

[428]*Id.* at 17.

imately 3.6 million subscribers.[429]

h) Bresnan Communications Group, LP and TCA Cable Partners II

Bresnan Communications Company, LP, and TCI are forming a new partnership, Bresnan Communications Group, LP ("BCG"). The new partnership will serve 615,000 subscribers. Bresnan will be the sole general partner and the managing partner with a 10% equity interest, TCI will have a 50% limited partnership interest and Blackstone Capital Partners III Merchant Banking Fund, LP, will have a 40% limited partnership interest.[430]

TCA Cable TV, Inc. and TCI formed a partnership, TCA Cable Partners II ("TCA II"), in which TCA holds an 80% general partnership interest, and TCI holds a 20% general partnership interest.[431] The partnership serves approximately 300,000 subscribers. A committee consisting of three TCA members and three TCI members governs TCA II. Management and operation decisions require a majority vote of the committee, while major matters require unanimous approval.[432] Bresnan and TCA argue that, despite TCI's equity involvement, TCA and Bresnan control the budgets, make the personnel decisions, and make programming decisions without TCI mandating any particular carriage.[433] TCI states that TCA manages the day-to-day operations of the general partnership for a fee, and that TCI provides programming

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[429]TCI Comments at 44.

[430]Bresnan *et al.* Comments at 3.

[431]TCI Comments at 49.

[432]Bresnan *et al.* Comments at 3-4 (major matters include fundamental changes to the partnership, significant purchases or sales of assets, and mergers, dissolution or bankruptcy).

[433]*Id.* at 13.

to the TCA II partnership through SSI for a fee.[434]

[434]TCI Comments at 49-50.

Statement of Commissioner Harold W. Furchtgott-Roth, Concurring in Part and Dissenting in Part

In the Matter of Implementation of the Cable Television Consumer Protection and Competition Act of 1992, Review of the Commission's Cable Attribution Rules, CS Docket No. 98-82.

I respectfully dissent from the adoption of these cable attribution rules. I agree, however, with certain decisions regarding cable reform. I thus dissent in part and concur in part in this *Report and Order.*

General Attribution Standards

The instant cable attribution rules are based primarily on the newly revised broadcast attribution rules. See supra at para. 11 (incorporating by reference the reasoning set forth in the *Broadcast Attribution Report and Order*). Those rules are, with a few exceptions, imported into the instant context.

For the reasons that I gave in my dissent from the broadcast attribution rules, I must also dissent from these counting standards. See Statement of Commissioner Harold W. Furchtgott-Roth, Dissenting in Part and Concurring in Part, *In the Matter of the Commission's Regulations Governing Attribution of Broadcast and Cable/MDS Interests, MM Docket No. 94-150; Review of the Commission's Regulations and Policies Affecting Investment in the Broadcast Industry, MM Docket No. 92-51; Reexamination of the Commission's Cross- Interest Policy, MM Docket No. 87-154* (rel. Aug. 6, 1999). In short, I believe that we should have taken these opportunities to simplify our attribution rules, instead of creating additional layers of regulation such as the equity- debt-plus test and reaching into heretofore uncharted areas such as pure debt instruments.[1]

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[1] I would also have allowed for *full* transferability of the interests grandfathered under this *Report and Order. Cf. supra* at para. 136.

With particular respect to the changes in the insulation criteria for partnerships, I am sympathetic to the concerns that motivate the Commission. I would prefer to address policy questions in the substantive rule on the horizontal limit, however, not in the context of the attribution rules. I fear that the "materially involved in programming activities" test will prove too subjective to be efficiently applied and enforced.

I am also troubled by the elimination of the single majority shareholder exception. As I made clear in the Broadcast Attribution Order, this rule provides at least some safe harbor to regulated entities in terms of attribution. Against the backdrop of our vastly complicated attribution rules, this exception -- whether or not I would have created it in the first instance -- operates to provide at least one clear instance where interests will not be attributable. Unless we intend to start from scratch and come up with a streamlined attribution system, I think we should retain the single majority shareholder exception.

In this regard, I must note, again, a yawning inconsistency between the broadcast item and this one: while we generally adhere to the broadcast attribution framework for cable, the Commission departs from that framework for the single majority shareholder rule in particular. If the policy reasons animating the rule are persuasive in broadcast, then they ought to work equally well here -- especially given that the Commission states that the industries are not so different that different attribution rules are needed, as noted above. I see no rational justification for retaining this exception for broadcasters but repealing it for cable operators, and I do not think the Order provides one.

Cable Reform Issues

I agree with the Commission's definition of the term "affiliate" for purposes of the LEC effective competition provision of section 623(1). See supra at paras. 120-125. In particular, while the Title I definition does not control in this context, I think it wise to exercise our discretion in light of Congress' definition, as the Commission does. I thus join in

this decision. I would have used the same test, however, for purposes of both the competing provider provision of section 623(l) and the cable-telco buy-out rule, cf. supra at paras. 126-132, and thus dissent from that decision.

STATEMENT OF COMMISSIONER GLORIA TRISTANI, DISSENTING IN PART

In the Matter of Implementation of the Cable Television Consumer Protection andCompetition Act of 1992, Implementation of the Cable Act Reform Provisions ofthe Telecommunications Act of 1996, and Review of the Commission's CableAttribution Rules, CS Docket Nos. 98-82 and 96-85

I dissent from the majority's decision to modify the insulation criteria for limited partnerships and to narrow the attribution standard for officers and directors. These changes are ill-conceived, arbitrary and will prove unworkable in practice.

First, the majority departs from established precedent without adequate explanation. In adopting the broadcast attribution standard for purposes of Section 613, the Commission found:

> [T]he objectives of the broadcast attribution model are consistent with our goals in establishing ownership standards for subscriber limits. In this regard, the broadcast attribution rules focus on ownership thresholds that enable a broadcast licensee to influence or control management or programming decisions. We believe these same issues are also relevant to addressing the concerns at issue in this proceeding relating to the ability of cable operators to unduly influence the programming marketplace.[1]

Just last year, the Commission reiterated these views on reconsideration.[2]

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[1] *See Second Report and Order,* 8 FCC Rcd 8565, 8581 (1993) (emphasis added). The Commission made a similar finding with respect to the channel occupancy limits. *Id.* at 8592.

[2] *See Memorandum Opinion and Order on Reconsideration and Further Notice of Proposed Rulemaking, Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992: Horizontal Ownership Limits,* 13 FCC Rcd 14462 (1998).

Thus, the Commission has repeatedly recognized that it is one entity's ability to influence or control the management or programming decisions of another entity that implicate the concerns of Section 613. The majority, however, acts as if it is writing on a blank slate by ignoring the ability to influence or control a partnership's management and focusing only on programming-related decisions. The majority does not claim that the broadcast criteria, affirmed by the Commission only two months ago, are wrong.[3] But nor does the majority attempt to explain why our prior precedent is wrong - i.e., why the broadcast attribution criteria really do not address the same issues regarding influence and control over management and programming decisions at issue here. Indeed, the majority would find any such attempt difficult, since, in enacting Section 613, Congress expressed many of the same competition and diversity concerns that underlie our broadcast ownership rules.[4]

The arbitrariness of the majority's decision is further evidenced by its failure to apply its new rules across-the-board. As noted above, the majority does not argue for a change in the broadcast attribution rules. Nor does the majority change the attribution criteria that apply to our other cable rules -- including the cable/SMATV cross-ownership ban, the cable-telco buy-out prohibition, and the competing provider prong of the effective competition test - that apply the broadcast attribution standard. Nor does the majority explain, if programming decisions are the only concern under Section 613, why it restricts its decision to limited partnerships rather than applying it to all corporate structures.

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[3] *See Review of the Commission Regulations Governing Attribution of Broadcast and Cable/MMDS Interests*, FCC No. 99-207 (rel. Aug. 6, 1999).

[4] For instance, Congress believed that unfair practices by large cable companies "could discourage entry of new programming services, restrict competition, impact adversely on diversity, and have other undesirable effects on program quality and viewer satisfaction." H.R. Rep. No. 102-628 at 43 (1992). Similarly, in express legislative findings, Congress determined that the cable industry's concentration posed potential "barriers to entry for new programmers and a reduction in the number of media voices available to consumers." 1992 Act, Sec. 2(a)(4), 106 Stat. 1460.

For instance, the majority does not explain why we should continue to attribute the interests of passive institutional investors, if those investors remove themselves from programming-related activities. If the attribution rules are changed for purposes of limited partnerships under Section 613, logically either the same revisions should apply to these other rules, or a good reason must be advanced why they should not. The majority does neither.

Finally, I fear that the majority's belief that "programming activities" can be neatly cordoned off from other management functions is illusory. In the real world, the ability to influence a partnership's core business activities inevitably involves the ability to at least indirectly affect the various activities, such as programming, in which the partnership is involved. Until today, the Commission has always recognized this common sense proposition. In particular, the Commission has always recognized that the potential influence of officers and directors is significant, and should be attributable to a broadcaster or cable operator whenever these individuals' duties relate to the media activities of the company.[5] Now, however, we are putting officers and directors in the untenable position of determining, on the fly, whether a particular budgetary or marketing decision improperly involves them in "programming-related activities." Worse, the public's right to the competition and diversity benefits of Section 613 depends on them making the right decision. The public interest should not hang by so thin a reed.

For these reasons, I dissent from today's decision to the extent it amends our attribution rules governing limited partnerships, officers and directors.

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[5] *See, e.g., Report and Order*, 97 FCC2d 997 (1984). 1999 WL 958602 (F.C.C.), 14 F.C.C.R. 19,014, 14 FCC Rcd. 19,014, 17 Communications Reg. (P&F) 1104.

IN THE MATTER OF IMPLEMENTATION OF SECTION 11(C)
OF THE CABLE TELEVISIONCONSUMER
PROTECTION AND COMPETITION ACT OF 1992
Horizontal Ownership Limits
MM Docket No. 92-264
FCC 99-289

Adopted: October 8, 1999 Released: October 20, 1999

THIRD REPORT AND ORDER

By the Commission: Commissioner Furchtgott-Roth concurring in part, dissenting in part and issuing a statement; Commissioner Tristani approving in part, dissenting in part and issuing a statement.

I. INTRODUCTION

1. This *Third Report and Order* resolves the issues regarding Section 76.503 of our rules (the "horizontal ownership rules")[1] on which the Commission sought further comment in its *Second Memorandum Opinion and Order on Reconsideration and Further Notice of Proposed Rulemaking* ("*Second Order on Reconsideration*" and "Further Notice") issued in this proceeding.[2] In the *Second Order on Reconsideration*, the Commission denied petitions to reconsider the horizontal ownership rules, which were adopted pursuant to Section 613 of the Communications Act[3] in the Second Report and Order issued in this proceeding.[4]

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[1]47 C.F.R.§76.503.

[2]*In re Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992: Horizontal Limits*, MM Docket No. 92- 264 (rel. June 26, 1998).

[3]Section 613 was adopted as Section 11(c) of Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460, 47 U.S.C.§533(f)(1)(A).

[4]*In re Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992: Horizontal Limits, Second Report and Order*, MM. Docket No. 92-264, 8 FCC Rcd 8565 (1993).

Section 613 of the Communications Act required the Commission to "prescribe rules and regulations establishing reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such a person, or in which such a person has an attributable interest."[5] In the Second Report and Order, the Commission promulgated horizontal ownership rules which provide that "no person or entity shall be permitted to reach more than 30% of all homes passed nationwide through cable systems owned by such person or entity or in which such person or entity holds an attributable interest."[6] In addition, the Commission decided to permit cable systems to reach up to 35% of all homes passed nationwide "provided [that] the additional cable systems, beyond 30% of homes passed nationwide, are minority-controlled" (the "minority-control allowance").[7]

2. In the *Second Order on Reconsideration*, the Commission also continued its stay of the effective date of the horizontal ownership rules pending a decision by the United States Court of Appeals for the District of Columbia Circuit on challenges to the horizontal ownership rules and Section 613.[8] The Commission decided that any parties over the horizontal limit must come into compliance with the rules within 60 days of a judicial decision upholding the statute and the rules.[9] However, in order to facilitate monitoring of a cable multiple system operator's ("MSO") ownership interests, the Commission lifted the stay

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[5]47 U.S.C.§533(f)(1)(A).

[6]47 C.F.R.§76.503(a). Under 47 C.F.R.§76.503(f), an "attributable interest" is defined by reference to the criteria set forth in the Notes to the Commission's cable cross-ownership rules, 47 C.F.R.§76.501.

[7]47 C.F.R.§76.503(b). For purposes of this regulation, "minority-controlled" is defined as "more than 50% owned by one or more members of a minority group." 47 C.F.R.§76.503(d).

[8]*Second Order on Reconsideration* at para. 75

[9]*Id.* at para. 77.

insofar as it applied to the information submission provisions of 47 C.F.R.§76.503(c).[10]

3. The rules and the statute were challenged in two different forums. In *Daniels Cablevision, Inc. v. United States,* the United States District Court for the District of Columbia held that Section 613(f)(1)(a) violates the First Amendment.[11] The Daniels court also decided that, because "there is substantial ground for difference of opinion" as to the constitutionality of the underlying statute, it would stay its proceedings and the issuance of any relief to the plaintiffs pending appeal. Time Warner then challenged the horizontal ownership rules in the District of Columbia Circuit in *Time Warner Entertainment Co., L. P. v. FCC.*[12] In August 1996, the District of Columbia Circuit consolidated the appeal of *Daniels* with *Time Warner.*[13] The District of Columbia Circuit held the consolidated appeals in abeyance pending the Commission's decision on the petitions for reconsideration.[14] Once the Commission issued the *Second Order on Reconsideration,* the District of Columbia Circuit lifted its stay on its consideration of the consolidated *Daniels* and *Time Warner* proceedings. The appeal is currently pending.

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[10]The existing certification requirements of Section 76.503(c) are triggered when any person or entity that holds an attributable interest in cable systems reaching 20% or more of homes passed nationwide acquires additional cable systems. In light of the stay of enforcement of the horizontal ownership rules, the Commission relieved MSOs of the Section 76.503(c) requirement that the MSO certify that no violation of the 30% limit will occur as a result of an acquisition. Until the stay is lifted, the certification should only specify the incremental change the acquisition makes in terms of the 30% of household passed standard, i.e. specifying the ownership in terms of homes passed before and after the acquisition is complete. *Second Order on Reconsideration* at para. 76.

[11]*Daniels Cablevision, Inc. v. United States,* 835 F. Supp. 1, 10 (D.D.C. 1993), *aff'd in part, rev'd in part, Time Warner Entertainment Co., LP v. FCC,* 93 F.3d 957 (D.C. Cir. 1996).

[12]*Time Warner Entertainment Co., L P v. FCC,* No. 94-1035 (D.C. Cir. 1994).

[13]*Time Warner Entertainment Co., LP v. FCC,* 93 F.3d 957, 979-80 (D.C. Cir. 1996).

[14]*Time Warner,* 93 F.3d at 979-80.

4. In the *Further Notice,* we requested comment on whether 30% remains the appropriate horizontal limit in light of any changes in market conditions since 1993, when the *Second Report and Order* was issued.[15] We sought comment on three specific issues. First, the current horizontal rules are based on the number of homes that a cable system passes (i.e., homes that could possibly subscribe to the cable system) rather than the cable system's actual number of subscribers. We asked whether we should amend the rules to base calculations on actual subscribers. Second, the horizontal ownership limits currently are calculated based on an MSO's share of cable subscribers. Given the growth of non-cable multiple video programming distributors ("MVPDs"), we asked for comment on whether the calculations should take into account the presence of all MVPD subscribers rather than cable subscribers alone. Third, we sought comment on the constitutionality of the minority-control allowance under *Adarand Constructors, Inc. v. Pena,* 515 U.S. 200 (1995) and whether there were alternative minority policies that might satisfy *Adarand's* standards.[16]

5. After analyzing the statute and the comments filed in response to the *Further Notice,*[17] we conclude that the following changes should be made in the rules:

- The calculation of the horizontal limit should be based on cable subscribers served rather than on cable homes passed;

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[15] *Further Notice* at para. 32. In *Second Report and Order,* we stated that we intended to review the horizontal limits every five years in order to determine whether they were still reasonable under new market conditions and continued to meet their policy objectives. *Second Report and Order* at para. 40.

[16] *Further Notice* at paras. 78-88.

[17] A list of commenters and the abbreviations used to refer to them herein is attached as Appendix A.

- The limit should include consideration of all MVPD subscribers rather than just cable subscribers;

- The number of subscribers a single entity is permitted to reach through cable systems it owns or in which it has an attributable interest should be limited to 30 percent of MVPD subscribers in the United States.

- An operator's horizontal share should not include cable subscribers that it serves through means other than through "incumbent cable franchises" so that a system operator may grow over the limit by overbuilding other incumbent cable operators; and

- The "minority-control" allowance in the existing rules should be eliminated.

6. These changes will make the rules easier to understand and implement, recognize the dynamic factors relating to the growth of the MVPD market, and allow cable ownership interests to increase as competition in the market increases. The new 30% rule, because it is now a share of MVPD subscribers rather than on cable subscribers alone, is effectively the same as a 36.7% cable subscribers limit using the measurement system in the previous rules. The minority-control allowance is being deleted in light of the fact that no party filed comments on this issue to argue that the allowance is effective, should be retained or might be beneficial, and in light of the possible constitutional issues that the allowance raised. Finally, we deny the request of one of the petitioners that we permit any transaction under contract prior to the release of the *Further Notice* to be continued regardless of the new rules. We deny requests to lift the stay of our horizontal ownership rules and reiterate that the rules will become effective immediately upon the court's issuance of a mandate upholding Section 613 and the rules. We decide that affected parties that are in violation

of the rules at such time must comply with the rules within 180 days after the court issues its mandate.

II. Background

7. Section 613(f) of the Communications Act requires the Commission to prescribe rules and regulations establishing reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such person, or in which such person has an attributable interest.[18]

8. Congress did not direct the Commission to use a mathematical formula in determining the horizontal limits. Rather, Congress directed in Section 613(f)(2) that, the Commission must consider and balance, among other public interest objectives, seven specific public interest guidelines in determining the appropriate horizontal limits. These public interest guidelines are:

> (A) ensure that no cable operator or group of cable operators can unfairly impede, either because of the size of any individual operator or because of joint actions by a group of operators of sufficient size, the flow of video programming from the programmer to the consumer;
>
> (B) ensure that cable operators affiliated with video programmers do not favor such programmers in determining carriage on their cable systems or do not unreasonably restrict the flow of video programming of affiliated video programmers to other video distributors;
>
> (C) take particular account of the market structure, ownership patterns, and other relationships of the cable industry, including the nature and market power of the local franchise, the joint ownership of cable systems and video programmers, and the various types of non-equity controlling interests;
>
> (D) account for any efficiencies and other benefits that

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[18] 47 U.S.C.§533(f)(1)(A).

might be gained through increased ownership or control;

(E) make such rules and regulations reflect the dynamic nature of the communications marketplace;

(F) not impose limitations which would bar cable operators from serving previously unserved rural areas; and

(G) not impose limitations which would impair the development of diverse and high quality programming.[19]

9. The 1992 Cable Act and its legislative history indicate heightened Congressional concern over horizontal concentration among cable operators. Witnesses at the congressional hearings, including representatives of the MSOs themselves, testified to the need for cable horizontal ownership limits to preserve competition and protect the public interest.[20] Congress was concerned that the concentration of cable systems in the hands of a few "media gatekeepers" could potentially bar entry to new programmers and reduce the number of media voices available to consumers.[21]

10. However, Congress also recognized that multiple system ownership could provide benefits to consumers. The *House Report* stated that cable industry consolidation had benefited consumers by allowing efficiencies in the administration, distribution and procurement of programming, and also noted that concentration of cable operators could promote the `introduction of new programming services by

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[19] 47 U.S.C.§533(f)(2)(A)-(G).

[20] *See, e.g., Report of the Senate Committee on Commerce, Science and Transportation*, S. Rep. No. 92, 102d Cong., 1st Sess. 34 (1991) ("*Senate Report*") (testimony of John Malone, TCI Chairman, regarding need for cable horizontal ownership limits).

[21] 1992 Cable Act, Section 2(a)(4); *Senate Report* at 32-33; see Section 613(f)(2)(G) (directing the Commission to impose no rule that would impair the development of diverse and high quality programming); *see also Report of the House Committee on Energy and Commerce*, H.R. Rep. No. 102-628, 102d Cong., 2d Sess. 43 (1992) (diversity of information sources) ("*House Report*").

providing capital and a ready subscriber base for new services.[22] The *House Report* also observed that large cable MSOs can take competitive and programming risks that smaller operators cannot.[23] Similarly, the *Senate Report* acknowledged that horizontal concentration could create efficiencies from lower transaction costs in carriage negotiations between programmers and cable operators.[24]

11. In the *Second Report and Order*, the Commission adopted a horizontal ownership limit prohibiting any person from having an attributable interest in cable systems that in the aggregate reach more than 30% of cable homes passed nationwide. We found that this 30% ownership limit struck the proper balance between: (1) ensuring that the structure of the cable industry nationwide limited the possibility that large cable MSOs might exercise excessive market power in the purchase of video programming; and (2) ensuring that the majority of MSOs could

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[22] *House Report* at 43.

[23] *Id.*

[24] *Senate Report* at 33. Beginning in 1994, the Commission has issued annual reports on the status of competition in the delivery of video programming. In these annual Competition Reports, the Commission has noted the potential benefits as well as the potential competitive concerns of increased national horizontal concentration among cable MSOs. *See First Annual Report, In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, FCC 94-235, CS Docket No. 94-48, 9 FCC Rcd 7442 at paras. 148-155 (1994) ("*1994 Competition Report*"); *Second Annual Report, In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, FCC 95-491, CS Docket No. 95-61, 11 FCC Rcd 2060 at paras. 131, 146 (1995) ("*1995 Competition Report*"); *Third Annual Report, In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, FCC 96-496, CS Docket No. 96-133, 12 FCC Rcd 4358 at paras. 138-139 (1997) ("*1996 Competition Report*"); *Fourth Annual Report, In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, FCC 97-423, CS Docket No. 97-141 at paras. 140-14, 149 (rel. Jan. 13, 1998) ("*1997 Competition Report*"); *Fifth Annual Report, In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, FCC 98-335, CS Docket No. 97-141 at pa ras. 152-157 (rel. Dec. 23, 1998) ("*1998 Competition Report*").

continue to expand and benefit from the economies of scale necessary to encourage investment in new video programming services, diverse program offerings, and the deployment of advanced cable technologies.[25] In order to promote diversity of ownership, we also adopted the minority-control allowance, which allows an MSO to reach an additional 5% of homes passed by cable nationwide if these homes are reached by cable systems that are more than 50% owned by one or more members of a minority group.[26]

III. Basis for the Rules

12. Congress directed the Commission to establish horizontal rules; yet in response to the Notice in this proceeding and in the course of the judicial proceedings relating to Section 613, a number of commenters make arguments that, while sometimes couched as pleas for a higher limit, appear to challenge the legitimacy and rational basis of any regulations of the type Section 613(f) requires the Commission to adopt. They argue:

- that increases in channel capacity, through system upgrades and the introduction of digital channels, reduce the practical need as well as the ability of operators to select among alternative content sources;[27]

- that other rules, including mandatory broadcast signal carriage, channel occupancy, leased access, and public access rules, eliminate the need for ownership limits that are also designed to promote programming compe-

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[25] *Second Report and Order* at para. 25; *Second Order on Reconsideration* at paras. 37-42.

[26] *Second Report and Order* at para. 28.

[27] See, e.g., NCTA Comments at 9; TCI Comments at 26-27; Time Warner Comments at 17-18.

tition and content diversity;[28]

- that cable system operators as purchasers of programming content for their subscribers are bound by marketplace forces so that they acquire only that product which their subscribers demand and there is no evidence that cable operators have ever used their editorial discretion to deny an outlet for unorthodox or unpopular speech;[29]

- that, if any problems exist in this area, they can be addressed through ordinary antitrust enforcement processes.[30]

We are not persuaded that these arguments are responsive to Congress' concerns in adopting Section 613(f).

13. With respect to the channel capacity argument, system operators are implicitly suggesting that increased capacity translates into an increased demand for programming. This change in the supply and demand relationship between purchasers and sellers of programming would, it appears they are arguing, tend to mitigate concerns that are based on the buying (monopsony) power of system operators.

14. In most markets, a single incumbent cable operator is likely to have more than 80% of the multichannel video distribution market. Although calculations of market power are almost always complex, a frequently cited compendium of monopoly cases concludes that "market share in excess of 70% is almost always deemed sufficient to

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[28]See, e.g., TCI Reply Comments at 8, 12.

[29]TCI Comments in Docket 98-92 at 40 ("Investors will not tolerate actions designed to foreclose specific viewpoints or opinions merely for ideological purposes.").

[30]Adelphia *et al.* Comments at 29; Bresnan Comments at 26; TCI Comments at 67; Time Warner Comments at 23; Time Warner Reply Comments at 15.

support an inference of monopoly power, although that inference may be overcome by other evidence."[31] The cable television industry has become, in the words of the 1992 Cable Television Consumer Protection and Competition Act "A dominant nationwide video medium."[32] On the other hand, the programming supply market is extremely competitive with increases in cable channel capacity, with the growth rate of new programmers rapidly outpacing the growth of new channels.[33] The Commission's 1998 Competition Report found that there were 245 national cable networks and that 65 new cable networks were planned to launch in the near future.[34] The decreasing marginal value of additional channels, the more limited exposure these channels receive by virtue of their placement on digital or other tiers to which subscribership is restricted and the associated difficulties of attracting an audience base to support advertising sales all tend to suggest that capacity increases have not had the consequence suggested and that channel expansion has not negated the Congressional concerns. Cable operators still have the power to decide which cable networks will

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[31] *I Antitrust Law Developments* (Third) 213-214 (1992) (citations omitted).

[32] Public Law 102-385,§2(a)(3). *See also 1998 Video Competition Report* at para. 6 ("We find that cable television continues to be the primary delivery technology for the distribution of multichannel video programming and continues to occupy a dominant position in the MVPD marketplace.").

[33] *See* comments filed in *In re Carriage of the Transmissions of Digital Television Broadcast Stations, Amendments to Part 76 of the Commission's Rules*, CS Docket No. 98-120 ("Digital Carriage"); *e.g.*, Adelphia Digital Carriage Comments at 21 ("Even if technological advances result in a greatly increased number of channels on cable systems, the number of programmers competing for carriage on those channels increases at a faster rate."); NCTA Digital Carriage Comments at 47 ("[I]ncreased channel capacity continues to be outpaced by an increased number of national cable program networks."); Encore Digital Carriage Comments at 5; America's Voice Digital Carriage Comments at 14 (number of competitors will outstrip available channel space); Weather Channel Digital Carriage Comments at 13-15.

[34] *1998 Competition Report* at para. 152.

"make it" even as channel capacity grows.[35]

15. The suggestion that other statutory provisions and Commission rules effectively address the same concerns we find equally unpersuasive. We believe Congress passed Section 613 to address specific concerns regarding the development of the video-programming market. Since Congress was aware of the interplay between the horizontal rule and the other rules addressing programming, it is clear that Congress intended for all the rules to work together in a complementary fashion. In any event, we do not believe that the goals of Section 613 are addressed by other statutory provisions. The channel occupancy rules[36] adopted pursuant to Section 613 of the Communications Act are intended to address only that programming that is controlled through direct ownership rather than through purchase and apply only to channel capacity up to 75 channels. The leased access rules,[37] while intended to address some of the same kinds of concerns, require the programmer to pay for carriage, a model which thus far has not resulted in any significant amount of nationally distributed programming content being made available to the public. The must-carry requirement[38] applies only to broadcasters, not to other unaffiliated programmers. Moreover the content of the broadcast stations that are carried, even when carried pursuant to mandatory obligations, is not totally divorced in terms of ownership and editorial voice from the cable systems involved. There are significant common ownership ties between a number of the broadcast networks involved and cable television system operators, including for example, significant AT&T (Liberty) ownership interests in News Corp. (the Fox networks), Time

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[35]See *Senate Report* at 33 ("[L]arge MSOs have the market power to determine what programming services can 'make it' on cable.").

[36]47 C.F.R.§76.504.

[37]47 C.F.R.§76.970 et seq.

[38]47 C.F.R.§76.55 et seq.

Warner and MediaOne ownership in The WB network, AT&T (Liberty) ownership in Telemundo, and Comcast and AT&T interests in QVC and HSN. These statutory based requirements thus share common objectives with the horizontal rules and function in a mutually supportive fashion with them but the contention that they are less restrictive methods of accomplishing the same substantive result is not correct. None of these rules fully address the core concern of national programming content diversity to which the horizontal limits are directed.

16. The Commission specifically considered how the behavioral rules interact with the horizontal ownership rules when it adopted the rules in this proceeding.[39] The limit is a structural complement to the other access provisions.[40] Thus, for example, it was explained that the horizontal ownership rules limit the potential for anticompetitive abuses of purchasing power in areas outside of the core areas covered by the program access rules, such as programming contracts between cable operators and non-vertically integrated programmers or contracts involving programming that is not delivered to cable operators via satellite. In addition, structural regulations generally are more easily enforced and their violation more easily detected than conduct regulations. We recognize that a large market share does not in and of itself indicate that a firm or a collection of firms has the ability to exercise market power or engage in anticompetitive behavior.[41] The cable operators have presented no new arguments in response to the *Further Notice* that would alter these findings.

17. The suggestion that cable system operators are somehow involved in content decisions only as somewhat mechanical purchasing agents

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[39] *Second Report and Order* at para. 26; *Second Order on Reconsideration* at para. 42.

[40] 47 U.S.C.§628; 47 C.F.R.§76.1000 et seq.

[41] *See, e.g., In re Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier,* 11 FCC Rcd 3271 (1995). We also recognize that the courts have generally found that a firm can not successfully obtain a monopoly with less than a 30% market share. *Antitrust Law Developments* (Fourth) 298-99 and cases cited therein.

for their subscribers, without independent discretion over the nature of that product, is equally unavailing as a response to the concerns reflected in Section 613. Because there are more programming services available for distribution than there are cable channels to be used for distribution, systems operator inevitably must make judgments as to which services will be carried. Marketing and other economic considerations that involve both the desire to satisfy consumer demands and independent profit calculations certainly play a major role in programming distribution decisions. But there would also seem to be little doubt, especially when the value of programming content may be difficult to determine in advance of its distribution, that issues of judgment, showmanship, social conscience, and personal taste are also involved.[42] The cable television industry has programming expenditures of almost eight billion dollars annually.[43] If these expenditures were allocated evenly across the industry, a firm with 30% of the market would pay $2.5 billion annually for programming, making it one of the largest purchasers of entertainment programming in the world.

18. With respect to the argument that ordinary antitrust policies and enforcement are sufficient to address any legitimate issues raised, we fail to understand why the statutory provisions and policies incorporated into antitrust law should be favored over the more targeted legislative mandate incorporated in Section 613. We agree with Ameritech that, if Congress had intended for us to rely on an antitrust analy-

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[42]Cable operators frequently associate themselves with programming content that reflects well on their standing in the community but they have an equal ability to discourage carriage of popular content that does not suit their tastes. *See e.g., Broadcasting and Cable*, April 1, 1996, at page 14 regarding the decision of TCI to cease carrying one particular type of programming and the explanation of the desirability of doing so notwithstanding the adverse economic consequences. In this article, the company official who made the decision not to carry the program was quoted as stating, "I hope this costs us money because I think the company needs to know there's a price to be paid for taking a stance."

[43]NCTA Cable Television Developments, Fall 1998/Winter 1999.

sis by itself, it would have directed us to do so or would not have adopted Section 613.[44] Instead, Congress directed that the Commission, in setting the horizontal limit, consider "among other public interest objectives" seven specific factors, none of which involves an antitrust analysis.[45] Indeed, in enacting Section 613, Congress was aware that the cable industry at that time was far from being concentrated under a traditional antitrust analysis assuming a national market for cable competition, but nevertheless empowered the Commission to enact horizontal limits using a public interest analysis.[46] The *House Report* stated that a traditional antitrust analysis should not be the "sole measure of concentration in media industries:"

> Both Congress and the Commission have historically recognized that diversity of information sources can only be assured by imposing limits on the ownership of media outlets that are substantially below those that a traditional antitrust analysis would allow .... The Committee believes that concentration of media presents unique problems that must be considered by

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[44]Ameritech Reply Comments at 7 ("The Department of Justice must enforce the antitrust laws but the Commission must effectuate the policies of the Communications Act.").

[45]See Section 613(f)(2) (A)-(G).

[46]There are two prevailing measures of market concentration -- the four firm concentration ratio ("Four Firm Ratio") and the Hirfindahl-Hirschman Index ("HHI"). The Four Firm Ratio measures the percentage of the market captured by the four largest companies in the market. The HHI reflects the distribution of market share among all firms in a given market, giving proportionately greater weight to the market shares of the larger firms. A market is generally considered concentrated when one firm, or a small group of firms, has a sufficient share of the market to exercise power over it. The Justice Department considers an industry concentrated when the HHI exceeds 1800 (although an HHI that exceeds 1000 prompts further evaluation) or when the four firm ratio exceeds 50%. According to the 1992 *House Report*, the HHI for the top 20 MSOs was 491 and the Four Firm ratio for the largest MSOs was 36%, well below the Justice Department's threshold. See *House Report* at 42.

the Commission.[47]

19. In sum, we do not find persuasive arguments that the concerns leading to the adoption of Section 613 are adequately addressed by market forces or technical changes, are not significant enough to warrant remedial action, or are properly addressed through other regulatory mechanisms.

IV. Using Homes Passed or Actual Subscriber Numbers to Calculate the Horizontal Limit

A. Background

20. The rules adopted in the *Second Report and Order* were based on a formula that related homes passed by an individual cable operator to the total homes passed by all cable operators nationwide.[48] We stated that a homes-passed standard would calculate a more stable number than a subscribers-based system because subscriber numbers fluctuate more often than homes passed.[49] In addition, we noted the arguments by some commenters that a subscriber-based standard might deter a cable operator from adding additional subscribers within its current systems as the operator approached the limit.[50] In the *Further Notice,*

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[47] *House Report* at 42. To the extent commenters are simply urging that the rules we adopt should be informed by an antitrust type of analysis, we note that no party has provided a specific analytical framework whereby this might be accomplished unless it is to suggest that the aggregation of interests within the cable industry does not pose an antitrust concern. Because cable operators are frequently monopolists in their local area, traditional horizontal analysis may not find harm in mergers. To the extent that is the case it reinforces, rather than undermines, the need for a separate analysis based on the standards set forth in Section 613.

[48] 47 C.F.R.§76.503(a).

[49] *Second Report and Order* at para. 24.

[50] *Id.* at para. 19.

we again asked whether the horizontal limits should be based on the number of actual subscribers or the number of homes passed.[51] We noted that a subscriber-based standard might present a more reliable number and could be more accurately calculated. In addition, we stated that if we amended the rules to include all MVPDs in the calculation, a homes-passed standard would be difficult to implement because several MVPDs might pass the same homes and Direct Broadcast Satellite ("DBS") programming providers pass every home in the country.[52] In addition to requesting comment on the benefits of a subscriber-based system, we sought comment on whether an operator approaching the limit might stop taking new subscribers or whether it would be able to anticipate the need to sell one of its systems in order to stay within the limit. We also asked whether we should devise special rules to address situations where subscriber growth within an operator's current systems might push the operator over the 30% limit.

B. Discussion

21. We will amend our rules to base them on how many subscribers an operator serves. Although homes passed might be a more stable number in that it does not fluctuate as often as numbers of subscribers,[53] it is not as reliable as the number for subscribers because homes passed calculations are based on estimates whereas subscriber numbers are based on billing records.[54]

22. More importantly, the horizontal ownership rules are designed to gauge the market power that an operator could potentially assert in

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[51] *Further Notice* at para. 79.

[52] *Further Notice* at paras. 84-86.

[53] See CU Comments at 12.

[54] See Adelphia *et al.* Comments at 23; TCI Comments at 58-61; Time Warner Comments at 28; contra RCN Comments at 18; RCN Reply Comments at 14.

the national programming marketplace.[55] In situations where there is only a single multichannel video provider, whether subscribership or homes passed data is used is largely a mechanical issue in terms of the market power issue. The return received by the content provider could equally be based on a share of revenues received, subscribers served, or size of the community involved depending on the contractual and economic (risk sharing) relationships involved. As the market develops in terms of competition we believe, in contrast to the argument made by RCN and in agreement with the cable operators, that an operator's actual number of subscribers more uniformly and accurately reflects power in the programming marketplace than does the number of homes passed.[56] While an operator may pass a large number of homes in its franchise area, the operator could have a low penetration rate in that area due to competition from other MVPDs or other factors, thereby rendering the number of homes passed an inaccurate indicator of the operator's market power.[57] Moreover, an operator does not purchase programming for the number of homes that it passes, but rather for its actual number of subscribers; thus, an operator's share of subscribers more accurately reflects its market power.

23. In addition, our decision below to include non-cable MVPDs in the horizontal limits calculation further supports our decision to rely on subscriber numbers. More than one MVPD may pass the same homes, making it difficult to determine an MVPD's share of the MVPD market on a homes passed basis. Moreover, although DBS providers pass every home in the country, homes passed does not accurately reflect their market power because DBS providers only serve approxi-

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[55]TCI Reply Comments at 35-36; Time Warner Reply Comments at 18.

[56]See TCI Comments at 61; Time Warner Comments at 29; TCI Reply Comments at 35.

[57]See Adelphia *et al.* Comments at 24; NCTA Comments at 19; Time Warner Comments at 29; Adelphia *et al.* Reply Comments at 12.

mately 10% of MVPD subscribers.[58]

24. Any theoretical deterrence that a subscribers-based limit might pose to keep an operator from adding new subscribers when the operator reaches the limit[59] does not outweigh the benefits of a subscribers-based system and does not merit an exception to the limit. Based on this record, we find it more reasonable that an operator will be aware of its potential growth areas when making acquisitions such that it will not cease accepting new subscribers in existing systems for fear of passing the limit. In their comments, the operators set forth in great detail their plans for consolidating or clustering their systems in order to enjoy the economies of scale that a large subscriber base will give them. The operators argue that a larger subscriber base in a clustered system will enable them to lower costs, improve current services, offer telephony and internet, and develop regional programming networks, as well as provide other benefits.[60] Given their long-term business planning and stated interest in clustering, operators will know in advance which systems they intend to grow for a larger subscriber base and which systems they intend to sell. Accordingly, an operator with an interest in the economic efficiency of its clusters would likely plan in advance to divest itself of a system rather than forego adding subscribers to systems or clusters within the operator's growth plan.

25. Thus, we disagree with MediaOne and Time Warner that an exception is needed based on the need to reflect in the rules "the

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[58] *1998 Competition Report* at App. C, C-1.

[59] See, e.g., CU Comments at 11-12.

[60] Cablevision Comments at 13; TCI Comments at 49-53; Bresnan Comments at 5, 22-23 (cable modems and digital cable television); NCTA Comments at 9 (clustering reduces duplicative costs); MediaOne Comments at 14; Time Warner Comments at 10; Adelphia *et al.* Reply Comments at 6; Comcast Reply Comments at 6; Cablevision Reply Comments at 7. MediaOne also argues that clustering enables MSOs to advertise their services in order to counter competition from other types of MVPDs. MediaOne Comments at 14.

dynamic nature of the communications marketplace."[61] Once the rules are in effect, nothing in the record suggests that, under the dynamics of the marketplace, an operator might find itself suddenly surprised that it cannot take any more subscribers without violating the horizontal ownership rules. We also disagree with MediaOne that an exception is necessary to ensure that cable operators are not prevented from servicing previously unserved rural areas.[62] MediaOne has not shown how a subscribers-based method impacts a rural area any differently than it impacts an urban area. MediaOne argues that, without an exception, the horizontal limit might prevent cable systems from expanding to certain rural areas in violation of some franchise agreements. First, cable already passes nearly 97% of homes nationwide.[63] Second, an operator is on notice with regard to the horizontal ownership rules and its franchise obligations, and the horizontal rules will not prevent a cable system from fulfilling its franchise obligations. If a franchise agreement requires an operator to expand its subscribership such that the operator will violate the horizontal limits, then the operator must divest a system elsewhere in order to stay within the limits and to meet its franchise obligations.

V. Using Total MVPD Subscribership to Calculate the Horizontal Limit

A. Background

26. In the *Further Notice*, we proposed that the horizontal ownership rules reflect the presence of all MVPDs rather than cable MVPDs alone in order to reflect changes in the MVPD market and their impact on

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[61]See, e.g., MediaOne Comments at 31; Time Warner Comments at 27.

[62]See MediaOne Comments at 31.

[63]National Cable Television Association, Current Estimates, available at: <http://ncta.cyberserv.com/qs/user_pages/Dev(currentestimates).cfm> (96.60% of homes passed/TV households).

programming power.[64] We noted that the emergence of non-cable MVPDs diminishes an operator's market power over programming while conversely an operator's interest in non- cable MVPDs increases its market power.[65] We requested comment on whether such a revision would be consistent with the Commission's statutory authority under Section 613.[66] In calculating a cable operator's market share, we proposed that the numerator would contain the operator's cable subscribers plus that operator's non-cable MVPD subscribers, and the denominator would contain the total number of cable subscribers plus non-cable MVPD subscribers nationwide.[67]

B. Discussion

27. We conclude that it is appropriate under Section 613 to include all MVPD subscribers in the horizontal limits calculation in order to reflect changes in the marketplace since 1993. In order to encourage competition through overbuilding, however, we will not include cable subscribers that an MSO serves through non-incumbent cable systems, as that phrase is defined below. In the Commission's determination of the appropriate measurements under the horizontal ownership rules, Section 613(f)(2)(A) requires the Commission to ensure that a cable operator cannot, by virtue of its size or by acting in concert with other cable operators, unfairly impede the distribution of video programming.[68] Moreover, Section 613(f)(2)(E) requires the Commission to

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[64] *Further Notice* at paras. 79-80.

[65] *Further Notice* at paras. 80-81.

[66] 47 U.S.C.§533(f)(1)(A).

[67] *Further Notice* at para. 79.

[68] Section 613(f)(2)(A) provides, "[The Commission shall] ensure that no cable operator or group of cable operators can unfairly impede, either because of the size of any individual operator or because of joint actions by a group of operators of sufficient size,

consider "the dynamic nature of the communications marketplace."[69]

28. The MVPD marketplace has changed since 1993. In our *Competition Reports*, we have stated that the effect of horizontal concentration on programming should take into account the presence of all MVPDs:

> in assessing the impact that national concentration may have in the MVPD programming market, we believe that it is appropriate to consider the presence of all MVPDs and MVPD subscribers in national concentration figures, and not just cable MSOs and cable subscribers. As non-cable MVPD subscribership increases, the significance of DBS, MMDS and SMATV operators in the MVPD program purchasing market also increases.[70]

29. Although cable continues to be the primary source of multichannel programming, its share of the MVPD market fell to approximately 81.77% in June 1999,[71] from 85.34% in June 1998, and from 93.37% in December 1994.[72] Currently, DBS has a 12.47% market share, home satellite delivery ("HDS") has a 2.21% market share, MMDS has a 1.73% market share, SMATV has a 1.73% market share, and OVS has a 0.09%

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the flow of video programming from the video programmer to the consumer[.]" 47 U.S.C.§533(f)(2)(A).

[69]47 U.S.C.§533(f)(2)(E).

[70]1997 Competition Report at para. 150.

[71]Cable had 66,065,400 subscribers in June, 1999. Kagan, *The Cable Financial Databook, 1999*. The current total number of MVPD subscribers is approximately 80,792,800, based on an estimated 1.4 million MMDS subscribers, 1.4 million SMATV subscribers; 66,000 OVS subscribers, 10,078,000 DBS subscribers and 1,783,411 HSD subscribers. *See Kagan's Marketing New Media* at p.1 (Oct. 19, 1998); *1998 Competition Report* at App. C, C-1; SBCA Comments in response to *Notice of Inquiry. In re Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming*. CS Docket No. 99-230.

[72]*1998 Competition Report at* App. C, C-1. 1999 WL 958598 (F.C.C.), 14 F.C.C.R. 19,098, 14 FCC Rcd. 19,098, 17 Communications Reg. (P&F) 1158

market share.[73] Between June 1997 and June 1998, DBS grew from approximately 5 million subscribers to 7.2 million subscribers, an increase of almost 43%.[74] By June 1999, DBS had grown to 10.078 million subscribers.[75]

30. Given the past and expected future growth of non-cable MVPDs, we believe that it is consistent with Section 613's mandate to include all MVPD subscribers in both the denominator and the numerator when calculating an MSO's market share under the cable horizontal limits. We reject the argument that non-cable MVPDs should not be placed in the denominator because cable has certain types of competitive advantages over non-cable MVPDs.[76] Although we agree that cable is still dominant in the MVPD marketplace, non-cable MVPDs have a growing impact on that marketplace. Inclusion of both cable and non-cable MVPD subscribers in the denominator will reflect the dynamic nature of the marketplace and the diminishing market power of cable operators as non- cable MVPDs increase their subscribership.

31. Likewise, when calculating an MSO's horizontal ownership, inclusion of both its cable and non-cable MVPDs subscribers in the numerator will reflect the market power held by that MSO through its total number of MVPD subscribers, whether reached through cable or other MVPD systems. This rule recognizes the increased market power gained by an MSO through its non-cable MVPD subscribers. This rule thus serves the objectives of Section 613 by reflecting both the dynamic nature of the marketplace and the ability of an MSO to impede the flow of programming by virtue of its total number of subscribers.

32. This rule is also consistent with Section 613's directive that the Commission establish limits on the number of cable subscribers a

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[73]See note 71 supra.

[74]*Id.* at paras. 5, 12.

[75]See note 71 supra.

[76]See CU Comments at 7; RCN Comments at 16-17.

person may serve.[77] The rule will not limit the number of subscribers a cable operator may reach through alternative MVPD systems. It also will not apply to persons who have no attributable ownership interests in cable systems. This rule will create a sliding or adjustable cable horizontal ownership limit, under which the number of subscribers a cable operator is authorized to reach through cable systems would decrease in proportion with any increase in the number of subscribers that that entity reaches through other MVPD systems. Conversely, the cable horizontal ownership limit would be higher for a cable operator that reaches fewer subscribers through other MVPD systems. This sliding scale calculation will more accurately reflect a cable operator's potential monopsony power and the extent of its control in the MVPD marketplace as a whole.

33. In order to promote competition in the marketplace, we find it appropriate at this time to include in an MSO's horizontal limit only those cable subscribers that it serves through incumbent cable franchises. For purposes of the horizontal ownership rule, "incumbent cable franchise" shall mean all cable franchises in existence on the date this order is released, October 20, 1999, and all successors in interest to those franchises. An MSO's cable subscribers shall include all subscribers served by those incumbent cable franchises, regardless of when the subscribers were added to the incumbent cable franchise system.

34. This rule will continue to limit an MSO's growth through acquiring incumbent cable franchises where cable-programming power is dominant. On the other hand, the rule sets no limits on an MSO overbuilding "incumbent cable franchises," thereby encouraging competition, more outlets for programming networks and more choices for consumers. Thus, we find that the benefits of not counting customers served via overbuilding outweigh any potential anticompetitive impact on the programming marketplace.

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[77]See Section 613(f)(1)(A) of the Communications Act, 47 U.S.C.§533(f)(1)(A); TCI Comments at 59; TCI Reply Comments at 31; Time Warner Comments at 31; NCTA Reply Comments at 3.

35. For purposes of reviewing compliance with the horizontal ownership limit, parties may use any generally accepted industry data as to the total MVPD subscriber count. We recognize that not all of the data used by the industry is identical and that some degree of estimation and double counting may be involved. We see no need, however, for parties subject to the limit, or for our own enforcement purposes, to spend unnecessary time refining the data given that the rule itself is based on estimates. Accordingly, in reviewing compliance with the rule, we will accept any published, current and widely cited industry estimate of MVPD subscribership. We would expect any party nearing the limit to bring to the Commission's attention any acquisition that would place them in conflict with the rules in accordance with the reporting requirement of Section 76.503(g).[78]

VI. The Level of the Horizontal Ownership Limit

A. Background

36. In the *Second Report and Order* and the *Second Order on Reconsideration*, we found that a limit of 30 percent of households passed by all cable operators represented a careful balance between: (1) limiting the possible exertion by a cable operator of excessive market power in the purchase of video programming; and (2) ensuring that cable operators are able to expand and benefit from the economies of size necessary to encourage investment in new video programming technology and the deployment of other advanced technologies.[79] In the *Further Notice*, we requested comment on whether 30% remains the appropriate horizontal limit in light of any changes in market conditions since 1993,

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[78] See Appendix B.

[79] *Second Order on Reconsideration* at paras. 8, 37-42.

when the initial rules in this proceeding were issued.[80]

37. Because we agree with the cable operators that emerging non-cable MVPDs have an impact on the programming marketplace, we will, as discussed above, amend the horizontal limits rule to include all cable and non-cable MVPD subscribers in the calculation of the appropriate horizontal market. In addition, as discussed below, to the extent that cable operators have concerns regarding efficiencies of scale and competition with incumbent telephone service providers, we will permit cable operators to grow in size through overbuilding without counting subscribers reached in that manner towards an operator's horizontal limit. With these exceptions, which we will take into account in the calculation of the horizontal limit, the commenters have not presented any new or credible facts that would alter our conclusion regarding the need for and the considerations applicable to the adoption of an appropriate horizontal limit.[81] Although the theoretical underpinnings for the rule remain unchanged and we continue to believe a 30% rule is appropriate, the effect of changing to a calculation based on the total size of the MVPD market results in a significant relaxation of the rule. The rule we adopt, a cable subscriber limit of no more than 30% of MVPD subscribers, is equivalent to a 36.7% limit based on cable subscribership alone.[82] We find this change justified by

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[80] *Further Notice* at para. 32. In the *Second Report and Order*, we stated that we intended to review the horizontal limits every five years in order to determine whether they were still reasonable under new market conditions and continued to meet their policy objectives. *Second Report and Order* at para. 40.

[81] Indeed, there was little agreement among the commenters as to what the horizontal ownership limit should be. Commenters supported horizontal ownership limits ranging from 20% to 50%. See, e.g., RCN Comments at 13; Bresnan Comments at 28; MediaOne Comments at 30; TCI Comments at 65.

[82] See note 72 *supra*. Thirty percent of the current 80,792,811 total MVPD subscribers permits an operator to serve 24,237,843 subscribers. 24,237,843 divided by the current 66,065,400 total cable subscribers permits an operator to serve 36.69% of cable subscribers. We note that, according to NCTA, there are currently 67,607,910 total cable

the record and a consideration of the criteria specified in Section 613. Otherwise, however, we find nothing in the record that would justify upsetting the balance established in the initial rules. We discuss below the commenters' arguments regarding the cable operator's role as a media gatekeeper, competition, and the efficiencies of consolidation.

38. Guidelines A, B, C and G of Section 613(f) require the Commission to ensure that cable operators, unilaterally or in coordination, do not unreasonably restrict the flow of video programming to consumers and do not hinder the development of new programming from diverse voices.[83] When Congress enacted Section 613(f)(1)(A), it concluded that cable industry concentration may enable MSOs to exercise excessive market power, or monopsony power, to bar the entry of new programmers and to reduce the number of media voices available to consumers:

> The cable industry has become highly concentrated. The potential effects of such concentration are barriers to entry for new programmers and a reduction in the number of media voices available to consumers.[84]

In particular, Congress was concerned with the possibility that "media gatekeepers will (1) slant information according to their own biases, or (2) provide no outlet for unorthodox or unpopular speech because it does not sell well, or both."[85] At the time of the 1992 Cable Act, cable

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subscribers and 81,827,910 total MVPD subscribers. NCTA Comments in response to *Notice of Inquiry, In re Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming*, CS Docket No. 99-230. Using NCTA's numbers, 30% of all MVPD subscribers equals 36.31% of all cable subscribers.

[83] 47 U.S.C.§533(f)(2)(A),(B),(C) & (G).

[84] 1992 Cable Act,§2(a)(4); 47 U.S.C.§521 note; see also *Senate Report* at 33 ("[L]arge MSOs have the market power to determine what programming services can 'make it' on cable.").

[85] *Senate Report* at 32-33; see also Section 613(f)(2)(G) (directing the Commission to impose no rule that would impair the development of diverse and high quality programming); *House Report* at 43 (1992) (diversity of information services).

served over 56 million households representing over 60% of all television households.[86] As of June 1999 cable served more than 66 million homes, representing approximately 82% of all MVPD households.[87] Thus, cable television remains the primary source of information and programming for many households in the United States. The horizontal rule limits the extent to which one or a few operators could reduce the number of diverse programming voices in the United States.

39. In the search for appropriate decisional criteria on which to base the Congressionally mandated ownership limit, one important element of the equation is the issue of what limit will sufficiently assure that no single cable operator "or group of cable operators" can "unfairly impede the flow of video programming from the programmer to the consumer."[88] If the rule can help to assure that no single operator or group of operators can unilaterally determine the success or failure of a new programming service, then the rule can achieve one important congressional purpose.

40. In our *1996 Competition Report*, based on information supplied by program providers in proceedings before the Commission, we suggested that, to have a long term prospect for success, the initial subscriber requirement for a new channel would be at least 10 to 20 million households.[89] In our *1998 Competition Report*, we noted the conventional understanding that in the typical mass market, an advertiser supported programming network needs between 15 and 20 million subscribers in order to ensure its long-term viability.[90] Some have argued that a

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[86] 1992 Cable Act,§2(a)(3); 47 U.S.C.§521 note.

[87] See note 71 supra.

[88] 47 U.S.C.§533f)(2)(A).

[89] *1996 Competition Report*, 12 FCC Rcd 4358 at para. 135.

[90] *1998 Competition Report* at para. 152. *See also 1997 Competition Report*, 13 FCC Rcd 1034, para. 155 (1998) ("Conventional understanding in the cable industry appears to be that a successful launch of a new mass market, advertisers supported, national program-

cable network needs as many as 30 to 40 million subscribers in order to attract advertising dollars to ensure long-term viability.[91] In the context of other Commission proceedings, parties within the industry have urged that it is generally not possible for a new, niche cable network to break even until its distribution reaches 20 million subscribers.[92]

41. Staff analysis further supports 15 million as a minimum subscriber number for viability. In analyzing data consisting of 1988-98 subscription figures for 68 cable networks along with the launch date for each,[93]

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ming network -- that is, the initial subscriber requirement for long- term success -- requires that the new channel be available to at least fifteen to twenty million households.")

[91] *See CAB Report: The Big Picture Channel Crossings*, Mediaweek (Apr. 14, 1997) (real growth over time comes from advertising) (*CBS Stumbles in Cable Distribution Game*, Cable World at 8 (Aug. 3, 1998) ("Typically, an ad supported network needs 40 million subscribers to attract ad revenues."); *Cable Networks Get Choked in Channel Congestion: Even with Upgrades, Niche Contenders Outnumber Open Spaces*, The Kansas City Star at E-1 (Apr. 4, 1997) (any cable network reaching fewer than 30 million subscribers is not getting advertising dollars that will make them profitable); *Cartoon Network Tops 30 Million: Large Subscribership Helps Sell Advertising*, The Atlanta Journal and Constitution at 5-C (Oct. 1, 1996) ("Advertisers do not seriously consider most cable channels until they garner 30 million subscribers, say industry experts.").

[92] *Closed Captioning and Video Description of Video Programming*, 13 FCC Rcd 19973, para. 45 (1998) ("GSN argues that it is generally impossible for a new, niche cable network to break even until its distribution reaches 20 million subscribers ..."); see Joint Comments of Outdoor Life Network, Speedvision Network, The Golf Channel, BET on Jazz, and America's Health Network in In re Closed Captioning and Video Description of Video Programming, MM Docket No. 95-176, at 10 (filed Feb. 28, 1997); *In the Matter of Outdoor Life Network and Speedvision Network*, 13 FCC Rcd 12226, note 116 (1998) ("The Networks contend that at 20 million subscribers, they will achieve a level of distribution sufficient to attract volume purchases by national advertisers and to generate subscriber revenues that approach the level necessary to carry the Networks operating costs.").

[93] *See* Paul Kagan Associates, Inc., *Cable Television Household Growth 1988- 98*, Cable Program Investor at 12-13 (Mar. 15, 1999). In performing this particular calculation,

staff found that networks that survive for a long period of time almost always obtain more than 15 million subscribers. Of the 39 networks started in or before 1988, 38 had more than 15 million subscribers in 1998.[94] Thus, we find no basic disagreement as to the general requirement for a cable programmer to succeed and have a reasonable prospect for survival.

42. Although we believe the 15-20 million subscriber estimates are now generally accepted in the cable industry as evidenced by the cable industry's reliance on this target in their comments in this proceeding,[95] we acknowledge that they may not cover every type of programmer. Some programmers may need far more subscribers to be successful, while others may need far fewer,[96] depending on the particular programmer's programming costs, target audience, and financial strength. Nevertheless, in balancing the Section 613(f)(2) factors, we must adopt a standard of general applicability in determining the horizontal limit. To that end, for purposes of this analysis, we will assume that a new programmer needs 15 million subscribers in order to have a reasonable chance to achieve economic viability. We use the lower number 15 over 20 million as a baseline in order to counterbalance the competing objectives of Section 613 to recognize the dynamics of the marketplace and the efficiencies of size. Fifteen million subscribers are not an

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the staff discarded 4 of the 72 networks that Kagan surveyed: WTBS, WGN, the Disney Channel, and Q2. WTBS and WGN are both superstations and have compulsory licenses for carriage. The Disney Channel was a premium channel for much of its life, and Q2 is now defunct.

[94] *Id.*

[95] See, e.g., Time Warner Comments at 25 n. 68; TCI Comments at 76 n.122; Bresnan Comments at 25.

[96] Indeed, sixteen (24%) of the networks surveyed by Kagan had fewer than 15 million subscribers in 1998, and 14 of those 16 have been in business for three or more years. See Paul Kagan Associates, Inc., *Cable Television Household Growth 1988-98*, Cable Program Investor at 12-13 (Mar. 15, 1999).

absolute minimum for viability. It is instead a number of subscribers that provides a reasonable probability of long-term success for a cable network. Fifteen million subscribers represent approximately 18.56% of the MVPD market.

43. Using the 15 million-subscriber number, a programmer could still theoretically obtain the minimum necessary circulation even if one system operator held 35, 40, or even 80% of the market. We do not agree, however, with the position of the cable operators that this is the end of the analysis.[97] We disagree with the cable operators' assumption that the horizontal limit should be designed with only a single large operator in mind.[98] Congress was concerned not only by the behavior of a single operator, but also with the possibility that a group of operators might decline to carry the programmer. Section 613(f)(2)(A) specifically directs the Commission to

> ensure that no cable operator or group of cable operators can unfairly impede, either because of the size of any individual operator or because of joint actions by a group of operators of sufficient size, the flow of video programming from the video programmer to the consumer ....[99]

Thus, the horizontal limit must account for the possibility that a group of operators will collectively deny carriage to a new programmer, either by unilateral, independent decisions or by tacit collusion. The limit should be set at a level such that, if each member of the group reaches the horizontal limit, the operators' "collective market share" will still leave enough of the market available to the programmer so that the programmer has a reasonable chance of obtaining the subscribers it needs in order to become financially viable. The legislative assumption is not unreasonable given an environment in which all the

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[97]See, e.g., Bresnan Comments at 28; Time Warner Comments at 26.

[98]See, e.g., Bresnan Comments at 28 (cable network could still obtain 15-20 million subscribers even if limit were 50%); Time Warner Comments at 26.

[99]Section 613(f)(2)(A) (emphasis added).

larger operators in the industry are vertically integrated so that all are both buyers and sellers of programming and have mutual incentives to reach carriage decisions beneficial to each other. Operators have incentives to agree to buy their programming from one another. Moreover, they have incentives to encourage one another to carry the same non-vertically integrated programming in order to share the costs of such programming.

44. The limit should also take into account that both cable operators and cable networks benefit from having a certain number of large MSOs. The MSOs benefit from the efficiencies of economies of scale. The cable networks benefit in that, if a new cable network obtains carriage on one large MSO, it will incur significantly lower transaction costs.

45. Examining the horizontal limit from the cable network's perspective, given that 20% of the market is the share that a cable network must reach to ensure viability, and assuming that there is a public value in minimizing transaction costs, one could argue that 20% is a lower bound on the appropriate MSO limit. A 20% limit would preserve the possibility that a cable network could acquire its minimum subscriber level in a single negotiation. In addition, if 5 MSOs were to divide the market, the cable network would have five chances of obtaining carriage. This would also serve the public interest by maximizing the potential that there would be at least 5 voices.

46. However, it is unlikely that a network could, in fact, achieve 20 enetration via a single MSO that reaches 20% of total subscribers. First, some of the MSO's cable systems may lack channel capacity and will be unable to carry the cable network at all. Second, those systems of the MSO that have channel capacity may place the cable network on an upper or digital tier or on a premium channel that not all subscribers receive. A 20% limit might therefore be unreasonably small in terms of efficiency from the cable network's point of view.

47. In addition, we find no reason to believe that the remaining four MSOs, comprising 80% of the market, would collectively decline to carry the new cable network, thereby leaving the programmer with

only one MSO. Balancing the efficiencies of size against the possibility of group action,[100] we believe that assuming coordinated action by two operators rather than by three or more operators is appropriate at this time. Under this scenario, if two MSOs, comprising 40% of the market, declined to carry a new cable network, this would leave 60% of the market available to the network. However, giving the cable operators the benefit of the doubt, we do not believe that a cable network requires an open field of 60% of the market in order to secure the 15 million subscribers the new cable network needs on average to succeed.

48. In this regard, we will examine and weigh various market factors to approximate a typical cable network's probable rate of success of reaching subscribers through cable operators that do not flatly deny the cable network carriage. We reviewed cable industry literature to examine the subscriber numbers of cable networks and to determine whether there was any evidence of the market factors underlying such a rate. In analyzing Kagan's June 30, 1999 census of cable network subscribers, we found that the 72 networks contained in the census had an average carriage rate of 53% (with a range from 95% to 5%) of 80.8 million subscribers.[101] We also reviewed another census of cable networks published by Cablevision magazine. For the 105 surveyed networks for which subscriber numbers were available, the average carriage rate was 36% of the total of 80.8 million MVPD subscribers.[102] Thus, the appropriate success rate would appear to be between 36% and 53%. However, the Cablevision and Kagan censuses do not reveal how many subscribers a cable network actively attempted - but failed -- to reach. In addition, the censuses do not explain what market factors worked for or against a cable programmer's carriage rate.

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[100]See Sections 613(f)(2)(A)&(E).

[101]See Paul Kagan Associates, Inc., *Cable Network Census*: June 30, 1999, Cable Program Investor at 8 (Aug. 13, 1999).

[102]See *Cablevision* at 73-74 (July 19, 1999).

49. Nevertheless, our review of the market factors affecting a new programmer's entrance demonstrated support for an average rate of success between these percentages. A programming network's ability to obtain carriage on cable systems may be limited by market conditions such as the lack of channel capacity on certain cable systems,[103] the high cost of competitive entry,[104] the competitive advantages of networks carried by the largest MSOs,[105] the demographics of audiences in certain viewing areas, and other non-quantifiable factors, such as the programming tastes of particular cable operators.[106] In addition, given the process of selling cable service by tiers, even where a pro-

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[103] *See Digital Carriage Notice* at para. 45 n.113 (noting that, according to Nielson's Cable On-Line Data Exchange, approximately two-thirds of cable systems in early 1998 were channel locked); see also *See Popcorn: The Latest Indie to Die*, Multichannel News at 1 (Nov. 25, 1996); *New Nets: Tough Act to Open: Cable Television Launches Postponed*, Cablevision (Nov. 27, 1995 (network launches delay due to lack of channel capacity and tight finances); *Comcast Shuts Q2 for Style*, Multichannel News at 1, 60 (Aug. 31, 1998) (reached only 8 million subscribers and lost $50 million over two years); *CBS Stumble in Cable Distribution Game*, Cable World at 8 (Aug. 3, 1998) (CBS sells its share of Eye On People network stating that it could not justify the ongoing financial strain of supporting a start-up cable network).

[104] *See Closed Captioning Order on Reconsideration*, FCC 98-236 at para 54 ("[N]ew networks, especially in the early stages, frequently must pay for carriage, and struggle to become an accepted venue for national advertising. These economic circumstances create significant accumulated debt and deferred earning which must be recovered from revenues if the network is to remain viable."); *In re New England Cable News*, 9 FCC Rcd. 3231 at para. 35 (1994) ("It is not uncommon for new programming services to sustain losses for long periods of time before their investors see any return on investment."); see also notes 107-112 *supra*.

[105] See Dennis H. Liebowitz, *Buyer's Guide for Programming - Thanks to TCI*, News Corp., Cable TV and New Media Law & Finance, Feb. 1997, at 1 ("[T]he new math makes it more expensive to absorb the cost of launching a new network. In turn, this favors existing networks.").

[106] *E.g., Combat Sports May Face Ultimate Finish*, Broadcasting and Cable (May 12, 1997) (certain cable operators drove the sport ultimate fighting off their cable systems despite the sport's popularity with their customers).

gramming network is added to a particular system it is unlikely that all subscribers to the system will purchase the network. Comments in this proceeding demonstrate that even vertically integrated programming networks generally do not reach 100% of an affiliated operator's subscribers and that carried networks in general may reach as few as 10% or as many as 95% of an operator's subscribers.[107] Given these inherent roadblocks to carriage, we find that it is reasonable to assume that a programming network will have at the most a 50% success rate of overcoming these roadblocks with respect to each subscriber available to it.

50. Like the 15 million-subscriber figure, the 50% success rate figure is a rough attempt to quantify a multitude of business conditions that may vary widely from programmer to programmer. Some new cable networks may have a higher success rate if they are affiliated with existing networks or cable operators, while other new cable networks produced by parties new to the cable market may have a lower success rate. We believe that the 50% figure takes into account the varying factors for market entrance. Because we believe that a cable network has a 50% chance of successfully obtaining carriage, only 40% of the market need be available to a new cable network for it to reach the 15 million subscribers (or 20% of the market) it needs. Accordingly, it is not necessary to maximize the number of MSOs controlling 20% of the market or to protect 60% of the market for a new cable network. Moreover, given the limited benefit to the cable networks, a 20% cable horizontal ownership limit threatens to limit unduly an MSO's ability to achieve economies of scale.

51. Examining the limit from the cable operator's side, one could posit an 80% limit, which would leave 20% of the market available to an MSO that might carry the new network. This scenario has several problems. Cable networks selling programming to two such unequally sized MSOs may charge excessively low rates to the large MSO and compensate by charging excessively high rates to the small MSO, or

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[107]See, e.g., TCI Comments, Appendix A, Table A-1.

enter other contractual arrangements that harm the customers to the small MSO and pose significant monopsony concerns. Although, a 50% limit could lead to a more even duopoly, the weaknesses of such competition are well established. The probability of tacit collusion is higher with 2 competitors than 3 competitors. Moreover, Congress was concerned with a "reduction in the number of media voices available to consumers," and devising a rule that would allow only two MSO gatekeepers to select those voices does not meet the congressional mandate.[108] Finally, Congress was concerned with the possibility that a group of MSOs might together harm a programmer, and a 50% limit permitting two MSOs to unilaterally or collectively harm a programmer would not address this concern.[109]

52. A 40% limit would pose similar problems. Although a cable network would have a reasonable chance of success if it gained access to an MSO at the 40% limit, two MSOs at the 40% limit, representing a total of 80% of the market, might decline to carry the new network. Even assuming that the remaining 20% of the market was in the hands of one MSO and that MSO agreed to carry the programmer, it is highly unlikely that the programmer would reach 100% of that MSO's subscribers for the reasons stated above. In addition, if the remaining 20% of the market is fragmented among several cable operators, the cable network again would be highly unlikely to succeed given a 50% success rate at carriage.

53. Approaching a horizontal limit from these two ends, a 20% limit favoring cable networks and a 40% limit favoring cable operators, we select a 30% limit as a reasonable balance between the interests of the cable networks and the cable operators. We believe that adopting a limit between 20% and 40% is reasonable given that the tradeoffs for the cable networks and the operators are roughly even. Based on this analysis, a new programmer would have a reasonable chance of

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[108]See 1992 Cable Act,§2(a)(4).

[109]See Section 613(f)(2)(D).

success if 40% of the 80,000,000 subscriber MVPD market is available to it after two operators have denied it access to the other 60% of the market. In other words, a 30% limit on a single operator's size will thereby prevent two large operators from obtaining control over 60% of the market. Thus, even if two operators, covering 60% of the market, individually or collusively deny carriage to a programming network, the network will still have access to 40% of the market, thereby giving it a reasonable chance of financial viability. This leaves open the possibility that two MSOs at the 20% limit might exist that could carry the cable network. In addition, assuming that the remaining 40% of the market is fragmented, leaving 40% of the market available to the cable network will give it a reasonable chance of success, given that we conclude that a cable network has a 50% chance of obtaining subscribers that are not actively denied to it.

54. While permitting cable operators to obtain economies of scale, the 30% limit serves the salutary purpose of ensuring that there will be at least 4 MSOs in the marketplace. The rule thus maximizes the potential number of MSOs that will purchase programming. With more MSOs making purchasing decisions, this increases the likelihood that the MSOs will make different programming choices and a greater variety of media voices will therefore be available to the public.[110]

55. We conclude that a 30% limit would fulfill Section 613(f)(2)'s mandate to strike a proper balance between the dangers to new programmers and the benefits to cable operators of economies of scale. Under current market conditions, we find that a 30% horizontal limit provides a new programmer with a reasonable chance of success, even if the largest operators decline to carry it. We acknowledge that the new cable programmer who is denied carriage by the largest operators may be at a severe competitive and financial disadvantage in the marketplace given the declining marginal cost basis of the program-

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[110]See 1992 Cable Act§2(a)(4).

ming distribution business.[111]

56. The market power of large cable operators has the potential to prevent nascent cable networks from even launching and to cause current networks to fail. While the exercise of market power could result in lower negotiated programming costs for cable operators in the short run, it could also adversely affect the development of diverse and innovative programming in the long run. Studies have shown that increased horizontal concentration has both efficiency and negative market consequences.[112] New networks might not be able to operate successfully subject to the lower prices that large operators are able to demand by virtue of their size.[113] Launch costs for a new cable network are estimated to be between $100 to $125 million.[114] New networks often must initially pay for carriage.[115] In addition, although advertis

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[111]See Dennis H. Liebowitz, *Buyer's Guide for Programming - Thanks to TCI*, News Corp., Cable TV and New Media Law & Finance, Feb. 1997, at 1 ("[T]he new math makes it more expensive to absorb the cost of launching a new network. In turn, this favors existing networks.").

[112]Ford, G.W., and J.H. Jackson, *Horizontal Concentration and Vertical Integration in the Cable Television Industry*, 12 Review of Industrial Organization at 514 (1997) ("Ford and Jackson"); Chipty, T., *Horizontal Integration for Bargaining Power: Evidence from the Cable Industry*, 4 Journal of Economics & Management Strategy at 375-397 (Summer 1995).

[113]See Dennis H. Liebowitz, *Buyer's Guide for Programming - Thanks to TCI, News Corp.*, Cable TV and New Media Law & Finance, Feb. 1997, at 1 ("[T]he new math makes it more expensive to absorb the cost of launching a new network. In turn, this favors existing networks.").

[114] *Viacom to FCC: Go Slow on Access*, Multichannel News at 50 (Sept. 7, 1998); *Struggling to Hook Up Viewers*, LA Times at F1 (Apr. 29, 1996) (quoting media analyst David Londoner, of Schroder Wertheim, and Lee Masters, MTV founder and CEO of El); *Acquired or Original?: New Networks are Mak..g Different Decisions than Their Predecessors*, Multichannel News at 8A (Jan. 16, 1995).

[115] *Throwing Money Around*, Cablevision at 14 (Jan. 27, 1997) ("Animal Planet is paying for carriage.... Networks like Sundance Channel, Independent Film Channel, Outdoor Life, Speedvision and others are all going to have to start paying just to get on systems

ing revenue is critical for a cable network's long-term success, some industry analysts believe that new networks cannot attract significant advertising until they surpass at least 30 million subscribers.[116] In particular, niche networks targeting small audiences with specific interests have difficulty attracting advertising.[117] Given the significant amount of debt a new network must therefore carry before it begins earning affiliation and advertising revenues,[118] nascent networks may not launch and new networks may fail because of an inability to carry

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- that is, using money that traditionally went into programming."); *Swimming Upstream - Programmers Caught in TCI's Recovery Net*, Multichannel News at 1 (Nov. 18, 1996) (TCI charging $14 and $8 per sub to launch Fox News and Animal Planet, respectively); *Sci-Fi Tries Incentives to Fuel Growth*, Multichannel News at 10 (Oct. 5, 1998) (at close to 50 million subscribers, Sci-Fi channel is offering $2 to $3 in launch support and free carriage in some instances).

[116] *See CBS Stumbles in Cable Distribution Game*, Cable World at 8 (Aug. 3, 1998) ("Typically, an ad supported network needs 40 million subscribers to attract ad revenues."); *Cable Networks Get Choked in Channel Congestion: Even with Upgrades, Niche Contenders Outnumber Open Spaces*, The Kansas City Star at E-1 (Apr. 4, 1997) (any cable network reaching fewer than 30 million subscribers is not getting advertising dollars that will make them profitable); *Cartoon Network Tops 30 Million: Large Subscribership Helps Sell Advertising*, The Atlanta Journal and Constitution at 5-C (Oct. 1, 1996) ("Advertisers do not seriously consider most cable channels until they garner 30 million subscribers, say industry experts.").

[117] *See Explosion of Channels Upping Ante For Agencies, Electronic Media at 22 (May 19, 1997); Cable's Little Engines That Might: Niche Channels Search For Shows, Bucks And Eyeballs; Small Start-Up Cable TV Channels*, Broadcasting & Cable at 62 (Mar. 31, 1997) (niche networks are almost guaranteed lower ratings from advertisers).

[118] *See Closed Captioning Order on Reconsideration*, FCC 98-236 at para 54 ("[N]ew networks, especially in the early stages, frequently must pay for carriage, and struggle to become an accepted venue for national advertising. These economic circumstances create significant accumulated debt and deferred earning which must be recovered from revenues if the network is to remain viable."); *In re New England Cable News*, 9 FCC Rcd. 3231 at para. 35 (1994) ("It is not uncommon for new programming services to sustain losses for long periods of time before their investors see any return on investment.").

this debt.[119] The 30% limit recognizes this dynamic of the communications marketplace[120] and the dynamic's ability to foreclose new programming.[121] TCI's argument that consumers benefit from lower rates (as a result of lower programming costs enjoyed by large MSOs due to their bargaining power) takes into account only the efficiency effect of horizontal concentration.[122]

57. As discussed above, the most significant change in the MVPD market has been the increased market share of non-cable MVPDs. We agree with the cable operators that the horizontal limits should take into account the non-cable MVPDs' impact on the programming marketplace. We take this into account by adopting our proposal that the calculation of the horizontal market include the presence of all MVPD subscribers. Using the presence of all MVPD subscribers in calculating the horizontal limit results in a self-adjusting horizontal limit whereby an operator's market share decreases when the total number of MVPD subscribers increases. Because the calculation of the horizontal limit will now automatically self-adjust based on the market share of noncable MVPDs, we need not alter the 30% limit to take into account their market share.

58. Cable operators argue that the emergence of new cable networks

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[119] *See Popcorn: The Latest Indie to Die,* Multichannel News at 1 (Nov. 25, 1996); *New Nets: Tough Act to Open: Cable Television Launches Postponed, Cablevision* (Nov. 27, 1995 (network launches delay due to lack of channel capacity and tight finances); *Comcast Shuts Q2 for Style,* Multichannel News at 1, 60 (Aug. 31, 1998) (reached only 8 million subscribers and lost $50 million over two years); *CBS Stumble in Cable Distribution Game,* Cable World at 8 (Aug. 3, 1998) (CBS sells its share of Eye On People network stating that it could not justify the ongoing financial strain of supporting a start-up cable network).

[120] See 613(f)(2)(E) ("dynamic nature of the communications marketplace").

[121] See 613(f)(2)(G) ("impose no limitations that will impair the development of diverse and high quality programming"); see also 1992 Cable Act,§2(a)(4).

[122] Using FCC rate data, Ford and Jackson found that only a portion of these discounts is passed along to consumers in the form of lower prices. Ford and Jackson at 514.

in the face of the continued growth of TCI, which purportedly passed 41% of homes passed by cable nationwide as of September 1998, demonstrates that cable operators have not used and will not use their monopsony power to adversely affect the programming marketplace.[123] TCI also argues that, compared to cable systems that do not have affiliated networks, TCI favors carriage of unaffiliated networks. That argument is likewise not convincing.[124] TCI's data appears to demonstrate the opposite. TCI's economic data appears to show that, as of 1995, TCI had favored carriage of 68% (13 of 19) of its affiliated networks versus 54% (25 of 46) of unaffiliated networks.[125] We also note that TCI's economists concede that their analysis does not take into account differences other than vertical integration among the systems in their study.[126] In addition, contrary to the findings of TCI's economists, several economic studies have shown that vertically integrated operators show preferences for their affiliated networks and exclude competing networks owned by independent programmers.[127]

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[123]MediaOne Comments at 11; NCTA Comments at 4-6, 9; TCI Comments at 16-17; TCI Reply Comments at 33. NCTA notes that broadband cable Internet may also be able to provide programming similar to what is now considered to be television, thereby creating additional avenues for programmers. NCTA Comments at 13.

[124]See TCI Comments at App. A; Stanley M. Besen & John Woodbury, *An Economic Analysis of the FCC's Cable Ownership Restrictions* at 18-21 (Aug. 14, 1998) ("Besen & Woodbury I"); *see also* Time Warner Reply Comments at 3 (*citing* Besen & Woodbury I).

[125]Besen and Woodbury I at 20 n.16.

[126]*Id.*

[127]Waterman, David, W. and Wise, Andrew, *Vertical Integration in Cable Television* at 88 (1997); Riordan, M. and D. Salant, *Exclusion and Integration in the Market for Video Entertainment Delivered to the Home* (July 7, 1994); Chipty, T, *Vertical Integration and Market Foreclosure: Evidence from the Cable Television Industry* at 19 (Feb. 1994); Olson, J. and L. Spiwak, *Can Short-Term Limits on Strategic Vertical Restraints Improve Long-Term Cable Industry Market Performance*, Cardoza Arts and Entertainment Law Journal at 285-315 (1995).

59. TCI's argument regarding its 41% homes passed market share lacks credibility in light of its arguments that actual numbers of total MVPD subscribers should be used to calculate the horizontal limit rather than homes passed. As noted above, we now recognize that the effective cable subscriber limit will be approximately 36.7% in light of today's market structure. Using these new methods of calculating the limit, TCI's market share would more likely approximate this limit. Moreover, TCI's argument does not take into account Section 613's mandate that we consider the possibility that two MSO's might foreclose a new programmer. In addition, WCA and Ameritech proffer credible evidence that indicates that MSOs have used their market power to cause unaffiliated programmers to refuse to sell their programming to other MVPDs. This evidence demonstrates another way in which MSOs can use their size and market power to impede the flow of programming to consumers in contravention of Section 613(f)(2)(A).[128] It is reasonable to assume that an unaffiliated programmer carried on a large MSO, with all the advantages that such carriage confers, would be disinclined to alienate the MSO by seeking carriage on a competitor.

60. While we agree with CU that a lower horizontal limit could promote competition through overbuilding,[129] we believe that 30% remains the appropriate limit to achieve these goals in light of the economies of scale it permits.[130] Competition will provide more ave-

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[128]Section 613(f)(2)(A) directs the Commission to devise rules that prevent MSOs from impeding the flow of programming to consumers. Ameritech and WCA state that, because of the MSOs' monopsony pressure, unaffiliated cable networks such as Fox News, MSNBC, Game Show Network, Eye on People, Home & Garden Television and TV Land act like vertically-integrated programmers and refuse to sell their products to alternative MVPDs. WCA Comments at 16; Ameritech Comments at 15; WCA Reply Comments at 5-10; see also CU Comments at 8 (stating that Viacom refused to provide its programs, such as Showtime, to People's Choice, a wireless cable company).

[129]CU Comments at 5.

[130]See *Second Order on Reconsideration* at para. 40

nues for programmers to reach subscribers.[131] The 30% limit may serve to facilitate the development of competition in those markets where cable operator market power already exists. By limiting the ability of large cable MSOs to merge or acquire incumbent cable systems, resulting in one or two MSOs controlling local cable market nationwide, the horizontal limit encourages cable operators to overbuild one another. Limiting this merger and acquisition potential may preserve opportunities for entry by overbuilders or other MVPD providers and reduce the likelihood that large MSOs can coordinate their behavior by mutually forbearing from overbuilding each other's service territories.[132] Coordinated activity between cable operators, whether tacit or overt, is more likely with few firms than many (due to greater ease in reaching a consensus, monitoring compliance, and punishing cheaters), and such behavior will have a greater impact the larger combined share of the market these firms control. Operators may use their market power to cause unaffiliated programmers to refuse to sell their programming to other MVPDs, thereby impeding the flow of programming to the consumer in contravention of Section 613(f)(2)(A).[133] The 30% limit also reduces the likelihood of coordinated activity between large cable MSOs in areas such as program purchasing, Internet services, and

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[131]See Section 613(f)(2)(A).

[132]See Section 613(f)(2)(c) (directing the Commission to take account of the market structure, ownership patterns and relationships within the cable industry).

[133]Section 613(f)(2)(A) directs the Commission to devise rules that prevent MSOs from impeding the flow of programming to consumers. Ameritech and WCA state that, because of the MSOs' monopsony pressure, unaffiliated cable networks such as Fox News, MSNBC, Game Show Network, Eye on People, Home & Garden Television and TV Land act like vertically-integrated programmers and refuse to sell their products to alternative MVPDs. WCA Comments at 16; Ameritech Comments at 15; WCA Reply Comments at 5-10; see also CU Comments at 8 (stating that Viacom refused to provide its programs, such as Showtime, to People's Choice, a wireless cable company).

equipment purchasing (e.g., set top boxes and converters).[134]

61. If the sole guideline in adopting rules were to encourage the largest number of sources of editorial control possible, the horizontal limit would be quite low. Guidelines E and F of Section 613(f)(2), however, require the Commission to include in the rulemaking balance the efficiencies and benefits of consolidation and the dynamic nature of the communications marketplace.[135] In the *Second Report and Order* and in the *Second Order on Reconsideration*, we recognized and weighed the benefits of clustering and economies of scale and determined that 30% was the appropriate number to encourage growth without unduly raising competitive concerns.[136] We find no basis in this record to alter this balance. Cable operators argue that the limit should be raised so that they may compete with common carriers for the provision of Internet and telephony services.[137] However, under the current rules, a cable operator may obtain as much as 30% of the cable nationwide market. A 30% limit allows a cable operator to gain access to a substantial portion of the market to provide Internet access and telephony. The cable operators have presented no credible evidence that a larger size is necessary for the deployment of advanced technologies or telephony. Moreover, we note the possibility of cooperative arrangements among operators to offer coordinated telephony services through their cable

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[134]See generally, James L. Langenfeld and Louis Silvia, *Federal Trade Commission Horizontal Restraint Cases: An Economic Perspective*, ANTITRUST LAW JOURNAL (1993); Alexis Jacquemin and Margaret E. Slade, *Cartels, Collusion, and Horizontal Merger*, HANDBOOK OF INDUSTRIAL ORGANIZATION, Richard Schmalensee and Robert Willig, ed., (1990); see also NCAA v. University of Oklahoma, 468 U.S. 85 (1984); *Northwest Wholesale Stationers, Inc. v. Pacific Stationary and Printing Co.*, 105 S.Ct. 2613 (1985).

[135]47 U.S.C.§533(f)(2)(E) & (F).

[136]*Second Report and Order* at para. 25; *Second Order on Reconsideration* at para. 41; see also 1998 Competition Report at para. 144 (acknowledging the benefits of clustering).

[137]See, e.g., AT&T Comments at 10; Cablevision Comments at 20; TCI Comments at 53-56; MediaOne Reply Comments at 4; TCI Reply Comments at 15.

systems, so that a cable operator does not necessarily need to grow in absolute size beyond the limit in order to participate in the offering of a national telephony service.[138]

62. In addition, we disagree with the cable operators' arguments that the horizontal ownership rules prevent an MSO from clustering its systems in order to enjoy an economy of scale and to compete with the ILEC.[139] As we stated earlier in this proceeding, "[t]he 30% limit permits cable MSOs to cluster systems in order to gain efficiencies related to economies of scale and scope in administration, deployment of new technologies and services, extension into previously unserved territories, etc. Accordingly, the 30% limit simultaneously guards against the potential anticompetitive effects of horizontal concentration and allows cable MSOs to realize the benefits of clustering."[140] The horizontal limit permits an MSO to consolidate its systems in one area in order to compete with an ILEC, if it wishes to do so. If an MSO must divest a system in order to comply with the horizontal ownership rules, the MSO has the discretion to decide what cluster of systems to retain in order to serve its business plans and customers.

63. Ameritech and CU raise the negative aspects of clustering, observing that clustering may enable cable operators to deny their competitors access to affiliated video programming and may deter overbuilders.[141] RCN requests that we limit the size of cable clusters in order to

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[138]Paul Farhi, *Pact Ends MediaOne Bid War; Comcast Lets AT&T Buy Cable Rival,* The Washington Post (May 5, 1999) ("Comcast will allow AT&T to offer local telephone service to Comcast's cable customers." Agreement is dependent on AT&T reaching agreement with two other cable systems first.); Jarman, *AT&T Discusses Taking Over Cox Communication's Phoenix Telephone Service,* Knight-Ridder Tribune Business News (July 19, 1999).

[139]*See, e.g.*, MediaOne Comments at 30; NCTA Comments at 23.

[140]Second Memorandum Opinion and Order on Reconsideration at para. 41.

[141]See CU *et al.* Comments at 5; Ameritech Comments at 21; see also 1998 Competition Report at para. 144; *Second Order on Reconsideration* at para. 40.

promote competition.[142] In the *Second Report and Order*, we considered whether to adopt regional subscriber limits, but declined to do so.[143] We stated that other provisions of the Cable Television Consumer Protection and Competition Act of 1992 that were specifically designed to introduce local competition would better address issues regarding regional concentration.[144] In addition, there was no evidence in the record that indicated that any anticompetitive effects outweighed the potential benefits of cable clustering, such as regional programming, upgraded cable infrastructure and improved customer services.[145] Likewise, the record in this proceeding shows that the benefits of clustering - including market efficiencies and the deployment of telephony and Internet access services - outweigh any alleged anti-competitive effects on local programming.[146]

64. An additional cable operator argument in favor of a revised limit is that we that we should raise the cable horizontal limits to 35% because Congress raised the television broadcast station horizontal limits to 35%.[147] As indicated above, the practical consequence of including all MVPD subscribers in the base from which the limit is calculated is roughly equivalent to changing the rules to a 36.7% cable subscribers limit. We do not believe, however, that the commenters have shown how the broadcast station limits have any relevance to the cable horizontal limits. In contrast to the cable rules, the broadcast rules apply to single channel facilities where there are generally numerous

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[142]RCN Comments at 20.

[143] *Second Report and Order* at para. 16.

[144] *Id.*

[145] *Id.* at para. 17.

[146]Cablevision Comments at 13 n. 18; Bresnan Comments at 5, 22-23; TCI Comments at 49-53

[147]See, e.g., Adelphia *et al.* Comments at 29; Bresnan Comments at 25-26; MediaOne Comments at 40; Time Warner Comments at 24-25.

directly competitive broadcast outlets in the market. Because a broadcast station competes with other broadcast stations in a local market and viewers therefore have several options for television viewing, a broadcast station owner does not actually have 100% of the local market's viewers all of the time. Thus, a broadcast station owner at the 35% national ownership limit cannot be deemed to have 35% of the nation's broadcast television viewers all of the time. A cable system has a set number of viewers making it possible to calculate more specifically than broadcast the number of viewers a cable system owner serves at the national level. In Section 613, Congress set forth seven specific criteria for the establishment of cable horizontal limits, which the Commission has followed. In addition, we fail to see the relevance to this proceeding of the Commission rule allocating half of a television market to a UHF station.[148] That rule recognizes that a UHF station transmits a weaker signal than a VHF signal and likely is unable to reach an entire television market.[149]

65. Finally, we reject Adelphia *et al.*'s request that we not apply the rules to any transactions under contract prior to the release of the *Further Notice,* and that existing joint ventures not subject to TCI's managerial control be permitted to grow through limited acquisitions to gain efficiencies of clustering.[150] Parties have been on notice since the *Second Report and Order* was released in 1993 of the horizontal limit. For the reasons set forth in Section VIII below, the horizontal rules will become effective immediately when the District of Columbia Circuit issues a mandate upholding the rules and Section 613(f)(1)(A), and affected parties in violation of the horizontal rules at that time must comply with the rules within 180 days after the court issues its mandate.

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[148] 47 C.F.R.§73.3555(e)(2)(I).

[149] *Id.*

[150] See Adelphia *et al.* Comments at 32.

XI. Ordering Clauses

90. Accordingly, IT IS ORDERED, pursuant to Sections 4(i), 303 and 613 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 303 and 533, that the amendments to 47 C.F.R. §76.503 discussed in this Third Report and Order and set forth in Attachment B ARE ADOPTED. These amendments shall become effective 70 days after publication in the Federal Register, following OMB approval, unless a notice is published in the Federal Register stating otherwise.

91. IT IS FURTHER ORDERED that the August 17, 1999 Consumers Union, Consumer Federation of America, and Media Access Project's Motion to Vacate Stay of Enforcement of Horizontal Ownership Limits and other requested relief IS DENIED in its entirety.

92. IT IS FURTHER ORDERED that 47 C.F.R. §503(a)-(f) as set forth in Attachment B is STAYED until the United States Court of Appeals for the District of Columbia Circuit issues a decision upholding Section 613(f)(1)(A) of the Communications Act, as amended, 47 U.S.C. §533(f)(1)(A), and 47 C.F.R. §76.503, and affected parties in violation of 47 C.F.R. §503(a)-(f) will come into compliance within one hundred and eighty (180) days after the court issues its mandate.

93. IT IS FURTHER ORDERED that parties shall continue to comply with the reporting requirements of Section 503 of our rules, as modified by 47 C.F.R. §76.503(g) set forth in attachment B and as discussed in note 10 of this Third Report and Order.

94. IT IS FURTHER ORDERED that the Commission's Office of Public Affairs, Reference Operations Division, SHALL SEND a copy of this Third Report and Order, including the Final Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration in accordance with paragraph 603(a) of the Regulatory Flexibility Act, Pub. L. No. 96-354, 94 Stat. 1164, 5 U.S.C.A. §601 et. seq.

FEDERAL COMMUNICATIONS COMMISSION
Magalie Roman Salas
Secretary

Appendix B

Rule Changes

Part 76 of Title 47 of the Code of Federal Regulations is amended to read as follows:

PART 76 -- MULTICHANNEL VIDEO AND CABLE TELEVISION SERVICE

1. The authority citation for Part 76 continues to read as follows:

AUTHORITY: 47 U.S.C. 151, 152, 153, 154, 301, 302, 303, 303a, 307, 308, 309, 312, 315, 317, 325, 503, 521, 522, 531, 532, 533, 534, 535, 536, 537, 543, 544, 544a, 545, 548, 549, 552, 554, 556, 558, 560, 561, 571, 572, 573.

Section 76.503 National Subscriber Limits

1. Section 76.503 is amended by deleting paragraphs (a) through (f) and adding paragraphs (a) through (g) as follows:

(a) Subject to paragraph (b) of this section, no cable operator shall serve more than 30% of all multichannel-video programming subscribers nationwide through multichannel video programming distributors owned by such operator or in which such cable operator holds an attributable interest.

(b) Cable subscribers that a cable operator does not serve through incumbent cable franchises shall be excluded from the cable operator's limit.

(c) For purposes of this section, "incumbent cable franchise" means a cable franchise in existence as of October 20, 1999 and all successors in interest to these franchises.

(d) Subscribers that a cable operator serves through incumbent cable franchises shall include all subscribers served by those incumbent cable franchises, regardless of when the subscribers were added to the incumbent cable franchise system.

(e) "Multichannel video-programming subscribers" means subscrib-

ers who receive multichannel video-programming from cable systems, direct broadcast satellite services, direct-to-home satellite services, multichannel multipoint distribution services, local multipoint distribution services, satellite master antenna television services (as defined in §76.5(a)(2)), and open video systems.

(f) "Cable operator" means any person or entity that owns or has an attributable interest in an incumbent cable franchise.

(g) Prior to acquiring additional multichannel video-programming providers, any cable operator that serves 20% or more of multichannel video-programming subscribers nationwide shall certify to the Commission, concurrent with its applications to the Commission for transfer of licenses at issue in the acquisition, that no violation of the national subscriber limits prescribed in this section will occur as a result of such acquisition.

Note 1: Certifications made under this section shall be sent to the attention of the Cable Services Bureau, Federal Communications Commission, 445 Twelfth Street, S.W., Washington, D.C. 20554.

Statement of Commissioner Harold W. Furchtgott-Roth,
Concurring in Part and Dissenting in Part

In the Matter of Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992, Horizontal Ownership Limits, MM No. 92-264.

There is much to commend in this Order. I join in the decisions to change the basis of the limit from homes passed to actual subscribers; to include non- cable MVPDs in the limit calculation; to repeal the minority-control allowance; and to retain the stay of these rules pending resolution of related litigation. *See* Parts IV-V, VII-VIII. I must dissent, however, the Commission's refusal to raise the limit itself from the current rate of 30%. See Part VI.

The Level of The Horizontal Ownership Limit

I would have raised significantly the relevant rate for cable ownership past the 30% that the Commission today maintains. This rate has been in effect since 1993 and, as the Commission itself has documented in any number of proceedings, the increase in competition in the multichannel video programming market -- assuming that is even the right market, as opposed to all video programmers, the actual terminology of the statute -- has been at least substantial, if not explosive. The statute directs us to take account of these changes. See 613(f)(2)(E) (Commission should "reflect the dynamic nature of the communications marketplace").

This Order even acknowledges these intervening competitive developments in the context of the decisions to change the limit calculation. *See supra* at paras. 28-30. I do not think we can take notice of increased competition for purposes of those ancillary decisions but close our eyes to that same fact in the context of the limit itself. Increased competition either exists or it does not, and the fact of that competition is logically relevant to the calculation of the limit and the limit itself.

Even if one were not willing to admit increased competition since 1993, changes within the cable industry itself -- most significantly, the expansion of channels due to upgrades -- mitigate a cable operator's potential for market power.

Furthermore, the Commission just a few months ago concluded that growth in the communications industry warranted loosening of the broadcast ownership rules. *See generally Review of the Commission's Regulations Governing Television Broadcasting, Television Satellite Stations Review of Policy and Rules,* MM Docket Nos. 91-221, 87-8 (rel. Aug. 6, 1999). I would think that some deregulation -- in particular, revising upward the section 11(c) cap -- would have been equally appropriate for the cable industry.

In the attribution Report and Order adopted today, the Commission concludes that "the cable industry's ownership and management structures do not in any relevant way differ from those of the broadcast industry." *Review of the Commission's Cable Attribution Rules,* CS Docket No. 98-82, at para. 11 (adopted Oct. 8, 1999). While I disagree with that statement (the many differences between these particular industries, and thus their ownership and management, are patent, at least to me), I note it in order to highlight the incongruity of the Commission's reasoning in these related decisions. Apparently, the industries are similar enough that we should use the same attribution rules, but when it comes to deregulation, they should not be treated equally. This makes little sense to me.

Part of what contributes to the Commission's view that the limit cannot go any higher than 30% is a fundamental misunderstanding of the premise of section 613(f). The Commission approaches the statute as if it were the "Reasonable Guarantee of Success for Cable Networks Act." Hence, its analysis of the appropriate percentage limit starts with the number of subscribers it takes to launch a new network.

But the Act is not meant affirmatively to ensure that new cable networks have some minimum chance of success in the marketplace. Rather, its plain language reflects an intent to prevent cable operators from "unfair[ly] imped[ing] ... the flow of video programming from the

programmer to the consumer." 47 U.S.C. section 613(f)(2)(A). A cable network can fail to get off the ground for infinite reasons *other than* the exercise of monopsony power by cable operators. The statute is not meant to create a minimum chance of success for one group, but to prevent specific anticompetitive behavior by a different group. We thus should be focusing on what it means for a cable operator or operators to "*unfairly* impede" the flow of programming, but this Order never does that.

Moreover, the "flow" with which the statute concerns itself is of "video programming," not just cable network or even MVPD programming. "Video programming" is a statutorily defined term, *see id.* section 611(20) ("'video programming' means programming provided by, or generally considered comparable to programming provided by, a television broadcast station"), which includes vastly more than just cable network programming. When many paths exist for distributing video programming to consumers -- which there are -- cable operators' ability to impede anything is drastically undermined.

Finally, the constitutional concerns raised by the statute -- grave enough that a federal judge has deemed it violative of the First Amendment, see *Daniels Cablevision v. United States*, 835 F. Supp. 1 (D.D.C. 1993) -- also mitigate in favor of a more generous approach to the limit in order to mitigate the direct burdens on speech imposed by these regulations. A higher subscriber rate, while it might not solve the First Amendment problem, would at least alleviate some of the burden created by the limit.[151] But these rules impose as heavy a burden on speech as the previous ones.

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[151]I note also that, in this Order, the Commission continues to focus, just as it did in the first Order promulgating rules under this section, on the effect of the limit on the content of video programming, belying the claim that these rules are based purely on competition-related goals. *See, e.g, supra* at para. 17 & n. 44 (discussing concern that "unorthodox or unpopular speech is being denied an outlet" and noting that cable operators can (as is their editorial right under the First Amendment) "discourage carriage of popular content that does not suit their taste.").

The Calculation Of The Horizontal Ownership Limit

The foregoing said, I do concur in the separate decisions to base the limit on actual subscribers rather than homes passed, see supra Part IV, and to include non-cable MVPDs in the calculus, see id. Part V. Those decisions make common sense, in that they acknowledge the expanded range and intensity of competition to cable. They also provide some effective relief to cable operators and allow them some room to grow as the MVPD market further develops.

Ultimately, however, the cleaner and more straightforward approach would have been to simply raise the limit itself. Moreover, I would have increased the limit to a greater extent than do these changes to the formula. I support them, however, to the extent they provide some benefit to regulated entities.

The Minority Control Allowance

I also concur in the decision to repeal the minority control allowance. See id. Part VII. As I noted in the Notice of Proposed Rulemaking, this facially race-based provision is presumptively violative of the Equal Protection Clause. See Separate Statement of Commissioner Harold W. Furchtgott-Roth, Second Memorandum Opinion and Order on Reconsideration and Further Notice of Proposed Rulemaking, In re Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992: Horizontal Limits (rel. June 26, 1998) (discussing application of strict scrutiny to the allowance). Although the Commission chooses to repeal these regulations for reasons of practicality, it makes no attempt to defend the constitutionality of this rigid numerical preference and its supposed connection to programming content in light of either the record in this proceeding or relevant judicial precedent. That is probably wise, because the task is near

impossible, legally speaking.[152]

Administrative Stay Of The Rules

Finally, I concur in the decision to continue the stay of these rules pending resolution of the related litigation in the Court of Appeals for the D.C. Circuit. See supra Part VIII.

Still on the Commission's books, however, is the analog to the minority- control allowance in the channel occupancy context. That regulation allows a cable operator to commit "two additional channels or up to 45 percent of its channel capacity, whichever is greater," to affiliated programming services if those services are minority-controlled. 47 C.F.R. section 76.504(c). This regulation suffers from the very same infirmities under Adarand as the horizontal ownership minority-control allowance. It should also be repealed.

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[152]I note also that, in this Order, the Commission continues to focus, just as it did in the first Order promulgating rules under this section, on the effect of the limit on the content of video programming, belying the claim that these rules are based purely on competition-related goals. See, e,g, supra at para. 17 & n. 44 (discussing concern that "unorthodox or unpopular speech is being denied an outlet" and noting that cable operators can (as is their editorial right under the First Amendment) "discourage carriage of popular content that does not suit their taste.").

STATEMENT OF COMMISSIONER GLORIA TRISTANI, DISSENTING IN PART

In the Matter of Implementation of Section 11(c) Of the Cable TelevisionConsumer Protection and Competition Act of 1992 Horizontal Ownership Limits MM
Docket No. 92-264

I would have lifted the Commission's voluntary stay of its horizontal ownership rules. While the stay may have done little harm in 1993, when it was imposed, it now constitutes a serious threat to the orderly enforcement of our rules and an abdication of our responsibility to implement Congress' express statutory directives.

In the 1992 Cable Act, Congress provided that the Commission "shall ... conduct a proceeding" to establish horizontal ownership limits. In 1993, shortly before the Commission issued its rules, the district court found the horizontal ownership provision of Section 613 unconstitutional on its face.[1] Importantly, the district court judge stayed the effect of his ruling, thereby permitting the Commission to adopt and enforce horizontal ownership rules. Nevertheless, when the Commission adopted its rules shortly thereafter, it voluntarily suspended enforcement pending outcome of the Daniels appeal. The Commission has not always been so quick to abandon Congress' mandates. For instance, although a district court judge found Sections 271-275 of the Communications Act to be an unconstitutional bill of attainder,[2] the Commission continued to enforce those provisions under circumstances similar to those here, until the appellate court eventually reversed the lower court decision.[3]

It has now been seven years since Congress expressly directed the

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[1] *See Daniels Cablevision, Inc. v. United States*, 835 F. Supp. 1 (D.D.C. 1993)

[2] See SBC Communications, Inc. v. FCC, 981 F. Supp. 996 (N.D. Tex. 1997).

[3] *See SBC Communications, Inc. v. FCC*, 154 F.3d 226 (5th Cir. 1998).

Commission to establish horizontal ownership rules, and six years since the Commission opted to ignore that directive on its own motion. In 1993, the Commission's decision made little practical difference: no cable operator was close to the 30% limit and appellate review of the Daniels decision could be expected well before the limit was breached.

Times have changed. Now we are faced with the real possibility -- indeed, the virtual certainty, if all pending transactions are approved -- that a single cable operator, AT&T, will be significantly over the 30% cap, even under the liberalized rules being adopted today. Moreover, concentration issues will be squarely before us when we consider AT&T's proposed acquisition of MediaOne -- a decision that will likely come before the D.C. Circuit rules on the Daniels appeal. Without enforceable rules, the Commission will not be able to address the Section 613 ownership issue at the time of the merger review, but, assuming the merger is approved, will have to wait until the D.C. Circuit acts. Not to worry, the majority says: if the D.C. Circuit upholds the horizontal ownership limits, AT&T and others will be required to come into compliance within 180 days of the decision.

The majority's assurances give me little comfort because I do not believe its admonition about divestitures will ever be enforced.[4] This is not a criticism of the Commission, but a recognition of administrative reality. It is much easier to enforce rules on a going-forward basis than to reverse established "facts on the ground." Ultimately, to the extent that the Commission is forced to grant waivers or grandfather ownership interests that violate our rules, Congress' purposes in enacting Section 613 will be eviscerated.

It might be different if the Commission believed there were a substantial likelihood that it would lose on appeal, or if there were some reason to believe that the 30% cap had grown stale. But on August 13,

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[4]I note that the Commission's commitment appears to be waning already. In last year's Order on Reconsideration, the Commission insisted that cable companies be prepared to come into compliance with its rules within 60 days of a judicial decision upholding our rules. On its own motion, the Commission has extended that to 180 days.

1999, the Commission filed a brief in the D.C. Circuit describing at length how, under the applicable standard established in the Supreme Court's *Turner* decisions (which the *Daniels* court did not have the benefit of), the horizontal ownership provisions and the Commission's implementing rules are clearly constitutional. Nor is the 30% cap out-of-date: today's Order reaffirms the 30AEp based on a fresh record.

In the end, the issue of lifting the stay boils down to whether the Commission is serious about implementing Congress' express directive to establish reasonable horizontal ownership limits. Today's decision indicates that it is not.

FCC 93-332

IN THE MATTER OF IMPLEMENTATION OF SECTIONS 11 AND 13 OF THE CABLE TELEVISION CONSUMER PROTECTION AND COMPETITION ACT OF 1992

HORIZONTAL AND VERTICAL OWNERSHIP LIMITS, CROSS-OWNERSHIP LIMITATIONS AND ANTI-TRAFFICKING PROVISIONS

MM Docket No. 92-264
Adopted: June 24, 1993; Released: July 23, 1993

REPORT AND ORDER AND FURTHER NOTICE OF PROPOSED RULE MAKING

Comment date: August 23, 1993
Reply comment date: September 3, 1993
By the Commission: Commissioner Barrett issuing a separate statement.

I. INTRODUCTION

1. In this *Report and Order and Further Notice of Proposed Rule Making* ("*Report and Order/Further Notice*"), the Commission adopts regulations interpreting and implementing the anti-trafficking and cross-ownership provisions of the Cable Television Consumer Protection and Competition Act of 1992.[1] The Commission also solicits further comment on its proposals regarding the establishment of subscriber limits and channel occupancy limits required by the 1992 Act. The Commission issued a *Notice of Proposed Rule Making and Notice of Inquiry*[2] ("*Notice*"), in this

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[1]Cable Television Consumer Protection and Competition Act of 1992, Pub.L. No. 102-385, 106 Stat. 1460 ("Cable Act of 1992" or "1992 Cable Act").

[2]*Notice of Proposed Rulemaking and Notice of Inquiry*, 8 FCCRcd 210 (1992) ("*Notice*").

proceeding, which sought comment on the intended objectives and scope of the Section 11(a) cross-ownership restrictions and the Section 13 anti-trafficking provision of the 1992 Cable Act.[3] The *Notice* also sought comment on issues pertaining to the adoption of limits on the number of subscribers any one entity can reach through cable systems owned by such entity; limits on the number of cable channels that can be occupied by vertically integrated programmers ("channel occupancy limits"); and on the appropriateness of imposing limits on the degree to which multichannel video program distributors ("Multichannel Distributors") may engage in the creation and production of video programming, as prescribed by Section 11(c)(2) of the 1992 Act.[4]

2. Section 13 of the 1992 Cable Act adds a new Section 617 to the Communications Act of 1934, as amended,[5] establishing a three-year holding requirement for cable systems. This cable anti-trafficking rule, with certain exceptions, prohibits cable operators from selling or otherwise transferring ownership in a cable system within three years following the acquisition or initial construction of such system by such operator. Section 11(a) of the 1992 Cable Act modifies Section 613(a) of the Communications Act to prohibit the common ownership of a cable system and a multichannel multipoint distribution service

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[3]A list of commenters responding to the issues raised in the Notice, and the references to specific commenters used herein, are listed on Appendix A.

[4]Most commenters addressing the issue of establishing limits on Multichannel Distributor participation in the creation and production of video programming opposed establishing such limits at this time. Most commenters agreed with the Commission's tentative conclusion in the Notice that the objectives of any such restrictions are fully addressed by other provisions of the Act. *See* NCTA Comments at 36-37; Viacom Comments at 19-21; Time Warner Comments at 60-62; TCI Comments at 58; Liberty Media Comments at 9-11. The National Private Cable Association, INTV and Liberty Cable indicated that some limits may be necessary. These commenters, however, did not indicate the rationale for such additional restrictions. The Commission will address this issue, along with the other provisions of Section 11, in a *Second Report Order*.

[5]47 U.S.C. §537.

("MMDS") licensee or a cable system and a satellite master antenna television service ("SMATV"), separate and apart from any franchised cable service, within any portion of the franchise area served by that cable operator's system.[6] The anti-trafficking and cross-ownership provisions of the 1992 Cable Act contain no specific effective date and thus, pursuant to Section 28 of the 1992 Act, became effective on December 4, 1992.[7]

3. In summary, this *Report and Order/Further Notice* contains the following determinations. The Commission concludes that the Section 617 anti-trafficking restriction applies only to assignments and transfers of control of cable systems. Such transactions will be defined generally, by reference to the Commission's broadcast assignment and transfer of control standards used to implement Section 310(d) the Communications Act. The Commission will rely on local franchise authorities to monitor and exercise primary enforcement responsibility under the anti-trafficking rule. Cable operators seeking to assign or transfer control of a cable system are required to certify compliance with the anti-trafficking rule to the local franchise authority at the time such cable operators seek local transfer approval. Disputes regarding the validity of such anti-trafficking certifications, the applicability of the anti-trafficking rule to a particular transaction, or eligibility for one of the rule's exemptions will be handled by the Commission pursuant to the Section 76.7 special relief procedures.[8] The Commission further determines that the statute provides the Commission with authority

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[6]47 U.S.C. §533(a)(2).

[7]Section 617(e) imposes a 120-day limitation on franchise authority consideration of transfer requests for cable systems owned for three years or more. 47 U.S.C. §537(e). The 120-day period commences upon the submission of all information required by Commission regulations and by the franchise authority. The Commission adopts such regulations herein and thus, the 120-day limitation will not become effective until the effective date of this *Report and Order/Further Notice.*

[8]47 C.F.R. §76.7.

to waive the three-year holding period in the public interest and directs the Commission to grant such waivers in cases of default, foreclosure and financial distress. In addition, the Commission adopts a blanket anti-trafficking waiver for small systems, serving 1000 subscribers or less.

4. In connection with transfer requests for systems owned for three years or more, the Commission establishes a standardized transfer approval form, which a cable operator must submit to the franchise authority in connection with such transfer requests. The Commission's transfer approval form solicits information necessary to establish the technical, legal and financial qualifications of the proposed transferee and any information required by the franchise agreement or applicable state or local law. Upon the submission of a completed FCC assignment or transfer approval form and the necessary exhibits, the franchise authority will have 120 days in which to consider such transfer request. Local authorities may request additional information reasonably necessary to determine the qualifications of the proposed assignee or transferee. Such requests, however, generally will not toll the running of the statutory 120-day limitation on franchise authority consideration unless the franchise authority and the cable operator otherwise agree to an extension of time.

5. With respect to the Section 613 cable/MMDS cross-ownership restriction, we modify Section 21.912 of our Rules to implement the statutory restriction. We amend Section 21.912 to prohibit * MMDS cross-ownership only where a cable operator's actual service area and the MMDS protected service area overlap. In assessing cross-ownership, we will consider a cable operator to have an attributable interest in an MMDS licensee if such cable operator holds five percent or more of the stock of such licensee, whether voting or non-voting. We do not adopt a single majority shareholder exception, and all officer and director positions and general partnership interests will be attributable, as will limited partnership interests of five percent or greater, regardless of insulation. We retain the local programming exception under

Section 21.912 as it applies to leased channels, but eliminate the overbuild and rural exceptions.

6. We adopt a separate rule to implement the Section 613 cable/SMATV cross-ownership restriction. The Commission concludes that Congress intended a narrower restriction with respect to cable/SMATV cross-ownership. The rules we adopt prohibit cable operators from acquiring an attributable ownership interest in a separate SMATV service within the cable operator's actual service area. Cable operators are permitted, however, to construct a stand-alone or integrated SMATV system in their actual service area, provided such SMATV service is offered in accordance with the terms and conditions of the cable franchise agreement. The attribution rules we adopt for this purpose are the same as those established for the cable/MMDS cross-ownership restriction. We acknowledge that the statutory cross-ownership restriction prohibits cable/SMATV cross-ownership only in a cable operator's actual service area. Therefore, in the unserved portions of the franchise area, a cable operator is permitted to build or acquire a stand-alone SMATV system, provided such cable-owned SMATV systems are operated in accordance with the terms and conditions of the cable franchise agreement.

7. With respect to establishing subscriber limits as required by Section 613, we seek further comment on our proposal to adopt a national subscriber limit of 25% of homes passed and to attribute cable system ownership based on the same criteria that is used in the broadcast context. However, we continue to seek comment on establishing subscriber limits in the range of 20% to 35% of homes passed nationwide. In addition, we propose to permit ownership of additional cable systems, beyond the 25% limit, if such systems are minority-controlled.

8. We also seek comment on our proposal to adopt a 40% limit on the number of channels that can be occupied on a cable system by programming in which the particular cable operator has an attributable interest. We propose to define vertical attribution for this purpose by reference to the broadcast attribution criteria. In addition, we propose

to allow carriage of additional vertically integrated video programming services provided such video programming services are minority-controlled or are targeted to a minority audience.

IV. SUBSCRIBER LIMITS

A. Background

132. The 1992 Cable Act requires the Commission to establish horizontal ownership limits. Specifically, Section 11(c)(2) of the 1992 Cable Act requires the Commission to place limits on the number of subscribers an entity can reach through cable systems owned by that entity.[111] The establishment of these "subscriber limits" is intended to address Congress' concern regarding increasing horizontal concentration in the cable industry. Congress found that increased concentration in the cable industry had the potential to create barriers to entry for new programmers and to reduce the number of media voices available to consumers.[112]

133. In establishing the ownership limits mandated by Section 11, the 1992 Cable Act directs the Commission to consider the following public interest objectives of the legislation: (A) to ensure that no cable operator or group of cable operators can unfairly impede the flow of video programming from the programmer to the consumer; (B) to ensure that cable operators do not favor affiliated video programmers in determining carriage and do not unreasonably restrict the flow of video programming of unaffiliated video programmers to other video distributors; (C) to take account of the market structure, ownership patterns, and other relationships of the cable industry, including the market power of the local franchise, joint ownership of cable systems and video programmers, and the various types of non-equity controlling interests; (D) to take into account any efficiencies and other benefits that might be gained through increased ownership or control; (E) to ensure that such rules and regulations reflect the dynamic nature of the communi-

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[111] 47 U.S.C. §553(f)(1)(A).

[112] 1992 Cable Act, Section 2(a)(4).

cations marketplace; (F) to impose limitations that will not prevent cable operators from serving previously unserved rural areas; and (G) to impose limitations that will not impair the development of diverse and high quality programming.[113]

134. Proposal. Before imposing definitive horizontal ownership restraints on the cable industry, we want to be certain that in so doing we have struck the proper balance among the competing public interest objectives congress directed us to consider. Our review of the comments in response to the Notice has persuaded us that further comment on a number of matters is necessary before we can establish appropriate subscriber limits. However, the record to date has helped us to form certain tentative conclusions. Therefore, at this time, we seek further comment on our proposals regarding the appropriate threshold and application of the subscriber limits. In brief, we propose to adopt a national subscriber limit of 25% of homes passed and to attribute cable system ownership based on the same criteria that is used in the broadcast context.[114] However, we continue to seek comment on establishing subscriber limits in the range of 20% to 35% of homes passed nationwide. In addition, we propose to permit ownership of additional cable systems, beyond the 25% limit, if such systems are minority-controlled.

B. Applicable Market.

135. *Notice.* In the *Notice* we asked commenters to indicate whether regional or national subscriber limits, or both, were necessary to implement the objectives of the 1992 Cable Act. We noted that while

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[113]47 U.S.C. §533(f)(2). Congress intended these public interest considerations to apply to all ownership limits mandated by Section 11(c)(2), including the channel occupancy limits discussed *infra.*

[114]47 C.F.R. 73.3555 (Notes).

the legislative history of the 1992 Cable Act focused on national subscriber limits, it also discussed regional concentration. Additionally, we cited findings from the 1990 Cable Report, concluding that the level of national concentration in the cable industry did not warrant regulatory intervention, but indicating that regional concentration could lead to MSOs engaging in anti-competitive behavior on a regional basis without disrupting national markets.

136. Comments. Cable commenters addressing the issue of whether subscriber limits should apply to national and/or regional markets all favor establishing only national subscriber limits. Several cable commenters argue that the Commission lacks the authority to promulgate regional limits under the 1992 Cable Act. Additionally, they believe that national limits best serve the objectives of the 1992 Cable Act since most programming distribution occurs on a national, not a regional, basis. Also, these parties contend that regional limits would threaten the marketplace efficiencies afforded by regional concentration, such as expanded customer service and increased local programming.[115] Only INTV supports imposing regional subscriber limits, arguing that such limits are necessary to curb the anti-competitive power of MSOs in local advertising markets.[116] INTV would have the Commission prohibit a single cable operator from reaching more than 50% of the homes passed in a local market (as defined by Arbitron's

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[115] *See, e.g.* TCI Comments at 27-28; Time Warner Reply Comments at 2-5; NCTA Reply Comments at 5-6.

[116] INTV contends that in markets with only one cable operator, that operator is the conduit for all local advertising and therefore is in the position to dictate local advertising prices, which places other local media (*e.g.*, TV stations) at a considerable disadvantage. INTV Comments at 7-8. In response, cable commenters argue INTV's assertions are disingenuous since data shows that broadcast stations continue to control an overwhelming share of the local advertising market as compared to cable interests. *See* TCI Reply Comments at 19-20; NCTA Reply Comments at 12-13.

Area of Dominant Influence or ADI).[117]

137. Discussion. We propose to adopt exclusively national subscriber limits. We agree with the majority of commenters who conclude that national subscriber limits best serve the objectives of the 1992 Cable Act because most programming distribution occurs on a national, not a regional basis. We are also concerned that the imposition of regional limits may sacrifice many of the benefits and marketplace efficiencies associated with regional concentration, such as investment in the deployment of fiber optic cable, development of local and regional cable programming and improved customer service. Moreover, we are cognizant that denying cable operators the benefits of regional concentration could impede their ability to become competitors of local telephone companies.

138. Commenters are asked to indicate whether the proposed national subscriber limits would suffice to implement the objectives of the 1992 Cable Act. In addition, we would like commenters to consider whether the benefits of regional concentration outweigh the possible anti-competitive harm that such concentration may have on the local advertising and programming marketplace. Finally, we are concerned that if we impose regional limits, other multichannel video distributors may not be available to serve unserved subscribers in all communities. We ask commenters to address this issue as well.

C. Measurement and Percentage Limitation.

139. *Notice.* The *Notice* sought comment on the measure that should be used to implement subscriber limits. We indicated that subscriber limits could be defined either as a share of cable subscribers or as a share of homes passed. However, after consideration of the two standards, the *Notice* proposed adoption of a homes passed measure. We

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[117]INTV Comments at 8.

tentatively concluded that while a subscriber-based standard is the more traditional measure, a homes passed standard is more appropriate because: (1) it encompasses all television households for which a particular cable operator provides access to cable programming; (2) it is more stable than a subscriber-based limit; and (3) it encourages the addition of new subscribers.

140. The *Notice* also asked commenters to indicate what percentage of homes passed nationally would constitute a reasonable limit on horizontal concentration. Specifically, we proposed a limit in the range of 25% to 35% of homes passed and asked a series of other questions designed to discern the level of subscribership needed to successfully launch new cable programming services. We also questioned whether the audience reach limits of the broadcast multiple ownership or network-cable cross-ownership rules were relevant to determining subscriber limits in this proceeding.[118] Furthermore, we observed that the Senate Report suggests that Section 11 was not intended to require divestiture by any existing MSO. The *Notice* also invited comment on whether we should establish a minority ownership incentive similar to the one used in the broadcast context, which provides for increased ownership of broadcast stations representing up to 30% of the television households nationwide if such additional stations are minority controlled.[119]

141. Comments. Most commenters addressing the issue of how to calculate subscriber limits, favor measuring the audience reach of cable systems by a homes passed standard rather than a subscriber-based

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[118]The Commission's broadcast multiple ownership rules limit the audience reach of television stations in which a single entity can hold an attributable interest to 25% of television households nationwide. *See* 47 C.F.R. §73.3555. The network-cable cross-ownership rule provides that national television networks can own cable systems which reach 10% of the homes passed nationally. *See* 47 C.F.R. §76.501.

[119]*See* 47 C.F.R. §73.3555(d).

standard. For example, Liberty Media, NATOA, MPAA, INTV and TCI all agree that a homes passed standard is more appropriate because a measure based on the number of subscribers is unstable and may have the effect of discouraging subscriber growth.[120] NCTA supports a homes passed standard too, but also believes the standard should reflect the fact that cable operators facing "effective competition" are unable to impede the flow of programming. NCTA therefore suggests subtracting from the number of homes passed all households that are also passed by a competing distribution service.[121] Only Intermedia favors a subscriber-based measure for determining the size of a cable operation, arguing that a subscriber-based measure is more accurate and is necessary to determine whether there is effective competition.[122]

142. Time Warner and GTE advocate the use of alternative measures. Time Warner suggests calculating subscriber limits by measuring the cable operator's share of subscribers who have access to programming either by means of cable or through other multichannel video distributors.[123] According to Time Warner, this approach would provide a

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[120] *See* Liberty Media Comments at 32; NATOA Comments at 20; Discovery Comments at 8-9; MPAA Comments at 6; INTV Comments at 4; TCI Comments at 28-29.

[121] NCTA Comments at 15. Alternatively, NCTA would have the Commission measure a cable operator's size as a percentage of the number of subscribers served not just by cable systems, but by other distribution technologies as well. *Id.* at 15 n. 31.

[122] Intermedia Comments at 9.

[123] Time Warner would make this determination based on a percentage that has, (a) as its numerator, the number of cable subscribers served by the cable operator in question, and that has, (b) as its denominator, the sum of (i) the number of all cable subscribers nationally and (ii) the number of subscribers to other multichannel video programming distributors. Time Warner Comments at 18-19.

truer measure of an operator's ability to impede the flow of video programming than would any measure based solely on cable subscribership or cable homes passed. GTE proposes another approach that would determine the audience reach of a cable operator based on its "total franchise area homes." According to GTE, substantial portions of existing cable franchise areas are not wired and therefore cannot pass all homes that are authorized to receive service. Consequently, GTE believes a measure based on the entire cable franchise service area--even if part of the area is not wired--would encourage operators to expand service into unbuilt areas.[124]

143. On the issue of establishing a reasonable limit on horizontal concentration, cable commenters generally support a subscriber limit of approximately 40% of homes passed nationally.[125] Relying on marketplace experience, antitrust principles and other factors, these commenters contend that there is no basis on which to conclude that an

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[124]GTE Comments at 2. In its reply comments, Time Warner opposes GTE's suggested approach, arguing its would not accurately reflect an operator's ability to impede the flow of programming, which was Congress' concern in enacting the statute. Time Warner argues that where an operator has not laid cable, it can do nothing to prevent others from providing service. Moreover, Time Warner points out that unbuilt areas provide opportunities for alternative distributors such as SMATV, MDS and MMDS. Time Warner Reply Comments at 8-10.

[125]Discovery advocates setting subscriber limits at a level considerably higher than the present degree of horizontal concentration. According to Discovery, the Commission can determine at what percentage a cable operator may effectively preclude the success of a new cable service by identifying the penetration level that an alternative technology distributor needs to survive. Discovery points out that Congress defined "effective competition" in Section 3 of the 1992 Cable Act in terms of at least two unaffiliated distributors both of which have a subscriber base of more than 15% of the households passed. Thus, Discovery indicates that under Congress' own definition, effective competition can exist even when one operator has 85% penetration. Discovery Comments at 7-9.

MSO with a 40% market share can impede the success of new programming services. They urge the Commission to avoid strict horizontal ownership limits that could preclude the efficiencies and benefits that result from continued horizontal growth.[126] Furthermore, they believe that Congress did not intend for the Commission to impose limits that would force existing MSOs to divest.[127]

144. In support of their position that a 40% subscriber limit is reasonable, cable commenters argue that extensive subscriber penetration is

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[126]For example, Discovery states that if the Commission adopts strict subscriber limits, the impact would be to sharply reduce the revenues of the programmers carried by large MSOs, which could threaten the survival of many programming networks. Discovery Comments at 5-6. TCI also submitted a study concluding that strict limits on horizontal ownership could diminish the quality, quantity and diversity of available programming. TCI Comments at 15-17. *See also* Besen, *et al.*, "An Economic Analysis of the FCC's Proposed Cable Ownership Restrictions" (filed Feb. 9, 1993) ("Besen Study") (attachment to TCI Comments). The Besen Study finds that the aggregation of subscribership does not harm consumers because cable systems do not compete directly against one another. According to Besen, while a large subscriber base may increase the bargaining power of an MSO in dealing with program suppliers, it does not affect the diversity of programming selected and distributed or distort the allocation of resources to the production of programming. Besen Study at 22.

[127] *See, e.g.* Time Warner Reply Comments at 11-14.

not essential to the success of a new programming network. Time Warner, TCI and NCTA contend that many program services have flourished at subscriber penetration levels well below 60%.[128] Time Warner provides examples of several successful program services that began with low penetration levels and which gradually gained audience share as their product improved or their popularity grew.[129] Cable commenters also observe that many factors determine the level of audience penetration necessary to make a new program service an economic success, including the degree to which a service is supported by subscriber fees versus advertising revenues and the type of programming service involved.[130] Finally, cable commenters rely on

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[128]These commenters note that program networks such as Black Entertainment Television ("BET"), The Learning Channel, Bravo and Court TV have had great success with penetration levels of less than 30% to 40%. Time Warner Comments at 28-29; TCI Comments at 24-25; NCTA Comments at 16.

[129]Time Warner Comments at 27-28. For example, Time Warner notes that The Family Channel, which was launched in 1977 achieved less than 10% penetration of all cable homes by its second year of operation, achieved only 22.1% in its third year, but approached 60% penetration by its sixth year of carriage. Another example provided by Time Warner is Nickelodeon, which achieved only 15.1% penetration in its second year of operation and now enjoys over 90% penetration. *Id.*

[130]*See, e.g.* NCTA Comments at 17. Time Warner, for example, points out that a service that emphasizes license fees as a source of revenue may need less penetration than will a service that is primarily dependent upon advertising revenues. Additionally, Time Warner notes that the cost structure of the service will determine the revenue level (and will thus influence the degree of penetration) that the service must reach to achieve profitability. Thus, a service that offers relatively expensive programming (*e.g.*, recently released theatrical motion pictures) will have a higher cost structure, and will need to achieve greater revenues, than will a service that depends upon less expensive programming (*e.g.*, news and syndicated TV programs). Time Warner Comments at 25-26.

antitrust principles, arguing that a single firm cannot exercise monopoly power with less than 50% of the relevant market.[131]

145. In contrast to the cable commenters, MPAA advocates a 25% subscriber limit, which would effectively cap the largest MSO at its present level of concentration.[132] MPAA does not believe Congress intended for subscriber limits to be set above existing levels of horizontal concentration since it was existing levels of market power that prompted congress to take action. MPAA also challenges the use of traditional antitrust market concentration measures as a basis for adopting a 40% subscriber cap. According to MPAA, such antitrust measures are not an accurate determinant of MSO market power because most cable systems do not compete with one another in the program acquisition market. MPAA also challenges the contentions of several cable commenters that a 40% cap is reasonable because new program services can survive with less than 60% penetration of cable households. MPSS believes its proposed 25% subscriber cap is liberal enough since if more than one operator approaches the 25% concentration figure, an independent programmer may have its market access

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[131]NCTA Comments at 17; TCI Comments at 19-23; Time Warner at 21-23.

[132]MPAA conditions its support for a 25% subscriber cap on the Commission adopting reasonable program access, leased access and attribution requirements. Otherwise, MPAA states that it advocates a limit lower than 25%. MPAA Comments at 5. NATOA also advocates a 25% subscriber cap. NATOA Comments at 19. NATOA believes that for the Commission to adequately correct the market aberrations caused by the anticompetitive practices of current MSOs, such MSOS should be required to divest current holdings. *Id.*

limited to only 50% of homes passed.[133]

146. Only INTV advocates a subscriber limit lower than that proposed in the *Notice*.[134] Specifically, INTV believes a subscriber cap of no more than 10% is appropriate.[135] INTV calls for stricter horizontal ownership controls than are used in the broadcast context. According to INTV, such strict limits are necessary because cable operators (unlike broadcasters) face little or no competition in the local marketplace. INTV argues that its proposal is consistent with the intent of Congress to enact regulations that do not allow the status quo to prevail.[136]

147. Discussion. In adopting horizontal ownership limits we seek to balance Congress' concerns regarding the ability of the largest MSOs to preclude the launch of new programming services with the benefits

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[133]MPAA Reply Comments at 2-4.

[134]However, David Waterman of the Annenberg School for Communications submitted a study suggesting that MSOs with less than 25% of the homes passed nationally may still be able to unduly influence the programming acquisition market. *See* Waterman Comments at 3 and Waterman, "Local Monopsony and Free Riders In Information Industries" (filed Feb. 9, 1993) (Waterman Study) (attachment to Waterman Comments). Time Warner and other commenters challenged Waterman's conclusions, charging that his study erroneously assumes that cable programming networks need to reach all cable subscribers and that cable networks primarily offer original programming. *See, e.g.* Time Warner Reply Comments at 14-16.

[135]Recognizing that its proposal would force divestiture of existing MSOs, INTV suggests applying the 10% cap prospectively. INTV Comments at 7.

[136]Time Warner, Liberty Media, TCI and NCTA all criticize INTV's proposed subscriber limit. TCI, for example, argues that a 10% cap is at odds with Congressional intent, since such a strict standard would impair development of diverse and high quality video programming. TCI Reply Comments at 17. NCTA argues that a 10% limit would be "absurd," and claims that INTV fails to acknowledge Congressional findings regarding the benefits of horizontal concentration (*i.e.*, efficiencies in administration, distribution and procurement of programming). NCTA Reply Comments at 11.

to consumers that result from some degree of horizontal concentration. Consequently, we propose to adopt a horizontal ownership limit prohibiting any one entity from owning cable systems that in the aggregate reach more than 25% of all cable homes passed nationwide, although, we continue to seek comment on subscriber limits in the range of 20%-35%. We believe that a subscriber limit of approximately 25% may be appropriate to prevent the nation's largest MSOs from gaining enhanced leverage from increased horizontal concentration, while ensuring that MSOs continue to benefit from the economies of scale necessary to encourage investment in new programming services and the deployment of advanced cable technologies. We also favor a 25% limit because it will not require divestiture by any cable operator, which we believe would be disruptive to the cable industry. The legislative history of the 1992 Cable Act suggests that the Congress did not intend for our efforts to disrupt existing cable ownership relationships.[137] Nonetheless, before we adopt this specific limit, we want to be certain that we have fully considered all the marketplace implications of such a limit. Therefore, we invite further comment on establishing subscriber limits in a range of 20%-35%.

148. We note that we regard the 10% limit proposed by some commenters to be contrary to the legislative history since it would require divestiture by some cable operators and would sacrifice the efficiencies achieved by horizontal concentration. On the other hand, there is some indication in the record that a higher limit of 30%-35% would be reasonable to allow for future MSO growth without precluding the launch or success of new programming services. In setting a specific percentage limit, we seek to set the limit high enough to preserve the benefits of horizontal concentration, while ensuring that cable operators cannot impede the flow of video programming.

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[137] *See* Senate Report at 34 ("the legislation does not imply that any company must be divested").

149. We ask commenters favoring limits below 25% to indicate how such limits can be squared with the Senate Report's indication that divestiture of existing systems was not intended. In addition, these commenters are asked to discuss the effect that such divestiture would have on service to subscribers, programming carriage agreements, and on future MSO investment in new programming and technology. Conversely, we ask commenters arguing for a limit above 25% to discuss the effect that such limits will have on the ability of new programming services to obtain MSO carriage and to indicate the competitive rationale for a higher limit, given the lack of competition faced by most cable operators locally and in the program acquisition market. We also ask commenters to address the effect of the prohibitions on anti-competitive practices established under Section 12 and 19 of the 1992 Act on the appropriate level for subscriber limits.

150. We further propose to allow ownership of additional cable systems, beyond the limit ultimately adopted, provided such systems are minority-controlled. The Commission adopted a similar policy in the broadcast context in order to encourage increased minority ownership of media outlets. To date, no commenters have addressed this proposal. We ask commenters to indicate whether allowing such increased ownership is desirable to encourage minority ownership of cable systems as a means of encouraging diversity of programming. We also ask commenters to indicate the appropriate amount of such increased ownership.

151. As we indicated in the *Notice*, we believe that it is appropriate to measure subscriber limits as a share of homes passed rather than as a share of cable subscribers. Most commenters endorsed this standard, indicating that a measure based solely on the number of cable subscribers is not optimal because it is relatively less stable and would discourage increased subscribership. We prefer a homes passed standard because it more accurately measures a cable operator's potential reach, by encompassing all television households for which a particular cable operator has the ability to provide service. We ask commenters to

indicate whether this measure is reasonable and appropriate to our objectives.

152. Also, as referenced in the *Notice*, we propose to calculate compliance with the national subscriber limits by subtracting the number of homes passed by cable systems in areas where "effective competition"--as defined under the 1992 Cable Act--is established.[138] We question, however, whether we should include for this purpose the definition of effective competition that applies to cable systems subscribed to by fewer than 30% of the households in the franchise area. We ask commenters to address whether this definition of effective competition is relevant to the competitive concerns which underlie the establishment of subscriber limits. In addition, some commenters advocate more lenient approaches and, for example, ask us to subtract from the number of homes passed those homes that are also passed by a competing program distributor, regardless of whether "effective competition" is established. We ask commenters to indicate why a more lenient definition of effective competition would be appropriate for purposes of subscriber limits than for purposes of rate regulation since both provisions are concerned with establishing the threshold

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[138]Under Section 3 of the 1992 Cable Act "effective competition" is established where "(A) fewer than 30 percent of the households in the franchise area subscribe to the cable service of a cable system; (B) the franchise area is--(i) served by at least two unaffiliated multichannel video programming distributors each of which offers comparable video programming to at least 50 percent of the households in the franchise area; and (ii) the number of households subscribing to programming services offered by multichannel video programming distributors other than the largest multichannel video programming distributor exceeds 15% of the households in the franchise area; or (C) a multichannel video programming distributor operated by the franchising authority for that franchise area offers video programming to at least 50 percent of the households in that franchise area." *See* 47 U.S.C. §543.

level of competition at which cable operators will be deterred from engaging in anti-competitive practices. We invite commenters to discuss this issue, as well as our proposal to adopt a homes passed standard, and any other matters relevant to this recommendation.

D. Horizontal Attribution Standard.

153. *Notice.* The *Notice* questioned whether the broadcast attribution criteria, or some other ownership attribution criteria should be used to implement cable subscriber limits. In particular, we asked if there are other types of ownership interests, such as non-equity interests, that should be cognizable for purposes of determining ownership under our subscriber limits.

154. Comments. With respect to establishing attribution criteria for determining the application of the subscriber limits, cable commenters believe the Commission should focus on the ability of the cable operator to control programming choices. Accordingly, NCTA argues for an attribution standard based on actual stockholder or managerial control of a cable system.[139] In particular, TCI advocates an attribution standard that would (1) exempt ownership interests under 10% ownership; (2) attribute interests of 50% or more; and (3) prorate interests between 10% and 50% based on the number of subscribers served by the system.[140] Cable commenters generally oppose setting the attribu-

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[139]NCTA Comments at 21.

[140]TCI Comments at 13-14. TCI would also incorporate a single majority shareholder exception as is used in the broadcast context. *Id.*

tion standard at 5% as was done in the program access proceeding.[141] Time Warner, for example, argues that such a strict standard is inappropriate because a 5% interest holder is incapable of influencing a cable system's program choices.[142]

155. On the other hand, MPAA, BellSouth, INTV and GTE advocate a stricter attribution standard than is proposed by the cable industry. Specifically, MPAA favors adoption of the same attribution criteria that is used to determine system ownership in the broadcast context under Section 73.3555 of the Commission's Rules. MPAA believes this criteria has worked well in the broadcast area and contends that the Senate Report instructed the Commission to use the broadcast attribution model.[143] BellSouth urges the Commission to apply the same broadcast attribution model to the telephone, cable and broadcast industries.[144] INTV favors attribution standards similar to those used in the network-cable cross ownership rule. According to INTV, a 5%-10% attribution standard is warranted because cable operators enjoy a local

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[141] *See Program Access Report and Order*, 8 FCCRcd 3359 (1993).

[142] Time Warner Comments at 19-20. Time Warner also contends that Congress did not intend for the Commission to adopt such a strict attribution standard, noting that the Senate Report that preceded the 1992 Cable Act mentioned the broadcast standard under Section 73.3555 as a possible model for developing attribution criteria. *Id.*

[143] MPAA Comments at 6.

[144] BellSouth Comments at 2.

monopoly.[145] GTE supports establishing attribution standards similar or identical to those applied to the telephone industry in the cable-telco cross ownership rule and as amended in the video dialtone proceeding.[146]

156. Discussion. We propose to adopt attribution criteria similar to the broadcast attribution criteria contained in Section 73.3555 of the Commission's Rules. Generally, under the broadcast attribution criteria, all non-voting stock interests (including most "preferred" stock classes) are generally not attributable. All voting stock interests of 5% or more are generally considered attributable. There are several exceptions to the presumption of attribution created by this 5% benchmark. Most notably there is a single majority shareholder exception, which provides that minority interests will not be attributed where there is a single 51% shareholder. In addition, the interests of "insulated" limited partners are not attributed. We believe that application of these attribution criteria in the context of subscriber limits is appropriate since the same issues regarding influence and control over management and programming decisions are at issue here. However, we request further comment on whether all these criteria are appropriate and applicable in the cable context.[147] We also invite commenters to evaluate the relevance of any of the other provisions or exceptions contained in Section 73.3555 to this proceeding.

157. In favoring the use of Section 73.3555 attribution criteria, we note that the objectives of the broadcast attribution model are consistent

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[145]INTV Comments at 5-6.

[146]GTE contends that the cable industry possesses power in local video distribution rivalling or exceeding the power of local telephone exchange companies in voice transmission. GTE Comments at 3. *See* 47 C.F.R. §63.54 (cable-telco cross-ownership restriction). *See also Video Dialtone Report and Order*, 7 FCCRcd 5781 (1992). In the video dialtone proceeding, the Commission amended its cable-telco rule to permit ownership interests of up to 5% by telephone companies in video programmers. *Id.* at 5802.

[147] *See* 47 C.F.R. §73.3555 (Notes).

with our goals in establishing ownership standards for subscriber limits. In this regard, the broadcast attribution rules focus on ownership thresholds that enable a broadcast licensee to influence or control management or programming decisions. We believe this same approach is relevant to addressing the concerns at issue in this proceeding, which relate to the ability of cable operators to unduly influence the programming marketplace. We also note that the legislative history of the 1992 Cable Act supports the use of the broadcast attribution criteria.[148] Furthermore, the same attribution criteria are used in the network-cable cross-ownership rule.[149] We believe that use of this attribution standard in these related contexts supports use of the same standard in the context of cable horizontal ownership limits.

158. Several commenters advocate a stricter approach, such as the video dialtone attribution standard, which attributes 5% voting or non-voting stock interests without exception.[150] While such an approach is consistent with the attribution criteria used in other cable contexts (*e.g.*, program access and cable/MMDS and cable/SMATV cross-ownership), we conclude that such an approach is unwarranted in this context.[151] This strict standard was developed as a modification of the cable/telco cross-ownership restriction in order to allow limited participation by telephone companies in the provision of video pro-

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[148] *See* Senate Report at 80. The Senate Report indicates that the Commission should use the attribution criteria set forth in Section 73.3555 (Notes) of our Rules, or such criteria as the Commission deems appropriate in determining ownership under the subscriber limit regulations.

[149] *See* 47 C.F.R. §76.501.

[150] *See supra* paragraph 155.

[151] The Commission adopted a strict attribution standard to implement Section 19 of the 1992 Cable Act. Specifically, a cable operator with 5% or more of the stock of a programmer, whether voting or nonvoting, is deemed to hold an attributable interest in that programmer for purposes of the regulations implementing Section 19. *See Program Access Report and Order*, 8 FCCRcd 3359 (1993).

gramming. These strict attribution standards were designed to ensure competition among rival distribution technologies. In this proceeding, however, our aim is to prevent any one cable operator from impeding the flow of video programming, which we believe warrants less restrictive attribution criteria.

159. In addition, several cable interests advocate that our attribution standard should focus exclusively on control, since in the absence of control, an operator does not have the ability to direct a system's programming choices.[152] Specifically, cable commenters would apply an ownership standard based on stockholder or managerial control of a cable system. Our attribution rules have long recognized that parties that have less than a majority equity interest in a media property can influence management and programming decisions.[153] We see no reason at this time to diverge from this longstanding principal. We encourage commenters to discuss these conclusions.

160. Finally, we do not endorse TCI's proposal to that we adopt a prorated attribution standard for all stock interests above 10%. First such an approach assumes that a 10% equity threshold is appropriate. However, this issue is currently being considered by the Commission in a separate rulemaking proceeding.[154] Moreover, such an approach fails to account for *de facto* control situations, where holders of a minor-

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[152] *See* Time Warner Comments at 30-31. *See also* Discovery Comments at 19-20; NCTA Comments at 20-21; and Liberty Media Comments at 36-37. Time Warner argues "control" normally is achieved by majority stock ownership, but does not necessarily want the Commission to adopt a "bright line" control standard. Rather, it would have the Commission evaluate ownership relationships on a case-by-case basis to determine whether an operator is impeding the flow of programming.

[153] *See* 47 C.F.R. §73.3555 and 76.501. These provisions were last reviewed comprehensively in 1984. *See Report and Order* in MM Docket No. 83-46, 97 FCC2d 997 (1984) (*Attribution Order*), *reconsidered* 58 RR2d 604 (1985) (*Attribution Reconsideration Order*), *further reconsidered* 1 FCCRcd 802 (1986).

[154] *Notice of Proposed Rule Making and Notice of Inquiry*, 7 FCCRcd 2654 (1992) ("Capital Formation Proceeding").

ity interest exercise actual control over management and programming decisions. When such *de facto* control exists, access to all of a system's subscribers is affected, and therefore all subscribers should be attributed.

E. Jurisdiction and Enforcement.

161. *Notice.* The *Notice* asked commenters to address how compliance with the subscriber limits should be monitored and enforced. Noting that few cable systems are presently in the range of the proposed subscriber limit of 25%-35%, the *Notice* suggested that a system of certification may be sufficient to enforce such limits. We indicated that we could require cable operators upon transfer or assignment of a cable system to certify that the transfer or sale would not violate the subscriber limits (i.e., by resulting in ownership of cable systems whose combined subscribership exceeds our limit). We asked commenters to discuss the merits of certification and whether all cable systems or only the largest systems should be subject to such certification requirements. Alternatively, we indicated that we could enforce subscriber limits on a complaint only basis, whereby parties believing that a particular acquisition would violate the subscriber caps, would notify the Commission of the potential violation. Finally, we questioned whether waivers or exceptions to the subscriber limits should be used in some circumstances and whether we should periodically review the ownership limits to ensure that our regulations are responsive to dynamic nature of the cable industry.

162. Comments. Commenters responding to jurisdiction and enforcement concerns agree that the Commission should enforce the subscriber limits on its own initiative. NCTA and Time Warner argue that implementation of a complaint and certification process would be unnecessarily costly and burdensome.[155] They point out that no system is in immediate danger of violating the 25% subscriber limit proposed in the

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[155]NCTA Comments at 23-23; Time Warner Comments at 31-33.

Notice and that the Commission can readily enforce its limits using publicly available data. Time Warner specifically opposes an enforcement process that would direct complaints to the local franchise authorities. Time Warner argues that local franchise authorities do not have the resources or the experience to properly assess subscriber limit compliance matters.[156]

163. On the question of whether we should allow for waivers or exceptions in appropriate circumstances, Time Warner and NCTA suggest that such waivers or exceptions should be obtainable for expansion of service into previously unserved rural areas and for de minimis violations (i.e., when commercial circumstances temporarily place an operator over the limits).[157] In addition, MPAA, Time Warner and NCTA favor the Commission's proposal in the *Notice* for periodic review of the subscriber limits every five years.[158]

164. Discussion. We propose that the FCC should enforce the suggested subscriber limit. We believe that in enforcing the subscriber limits it may be unnecessary to institute a formal certification process, whereby all cable operators must verify upon transfer or assignment of a cable system that they are in compliance with our subscriber limits. Commenters have suggested and we agree that such a process would be unnecessary and unduly burdensome since only a few MSOs are close to the proposed 25% threshold. However, we request additional comment on whether such certification should be required for cable operators currently reaching 20% or more of homes passed. Alternatively, it may be possible for us to adequately monitor and enforce

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[156]Time Warner Comments at 31-33.

[157]Time Warner Comments at 34; NCTA Comments at 23 n. 50.

[158]MPAA Comments at 6-7; Time Warner Comments at 35; NCTA Comments at 23.

subscriber limits through the use of readily obtainable public information Cregarding cable system ownership. Commenters favoring such an approach should indicate whether the necessary information regarding cable system ownership and the share of homes passed by the largest MSOs is publically available and the appropriate source that should be used to obtain such information on a regular basis. In addition, we believe that the Commission, and not the local franchise authorities, are the appropriate entity to consider any complaints asserting that a particular MSO is in violation of the subscriber limits. We seek comment on these proposals.

165. Cable commenters have also requested that we waive or exempt MSOs from the subscriber limits in instances of de minimis violations (such as when an acquisition temporarily places a cable operator over the permissible number of subscribers) or when an MSO is seeking to expand service into an otherwise unserved rural area. We agree that waivers may be appropriate in these situations and propose to consider such waiver requests on a case-by-case basis. We invite commenters to discuss these conclusions and indicate whether waivers may be appropriate in other circumstances.

166. Finally, in view of the fact that the cable market is a dynamic and changing industry, we believe that periodic review of the ownership limits is necessary. As we proposed in the *Notice*, we plan to review the subscriber limits every five years to determine whether such limits are reasonable under the prevailing market conditions. Commenters responding to this issue generally favored a five year review. We invite further comment on this proposal and ask commenters to indicate whether review every five years will be adequate to ensure that our regulations are responsive to the dynamic nature of the cable industry.

D. Ordering Clauses.

244. Accordingly, IT IS ORDERED that pursuant to the authority contained Sections 2(a), 4(i) and (j) and 303 of the Communications Act of 1934, as amended, and the Cable Television Protection and Competition Act of 1992, Pub.L. No. 102-385, Part 21 of the Commission's Rules, 47 C.F.R. Part 21, and Part 76 of the Commission's Rules, 47 C.F.R. Part 76, ARE AMENDED as set forth in Appendix D below, and will become effective 30 days after their publication in the Federal Register, except 47 C.F.R. §76.502(i) which will become effective 90 days after publication in the Federal Register.

E. Additional Information.

245. For additional information regarding this proceeding, contact Jacqueline Chorney, Mass Media Bureau, (202) 632-6990.

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton

Acting Secretary

SEPARATE STATEMENT OF COMMISSIONER
ANDREW C. BARRETT

RE: Implementation of the Cable Television Consumer Protection and Competition Act of 1992--Cable Ownership

This *Report and Order* adopts regulations interpreting and implementing only the anti-trafficking and cross-ownership provisions of the 1992 Act, which: (i) establish a three-year holding period for cable systems, and (ii) prohibit cable operators from holding and MMDS license or offering SMATV service, apart from any franchised cable service, in portions of the franchise area served by the cable operator's cable system. The Further *Notice* of Proposed Rulemaking regarding horizontal ownership and channel occupancy limits seeks additional comment on various proposals prior to implementing these provisions of the 1992 Act.

With respect to the *Further Notice of Proposed Rulemaking*, I write separately to voice my concern regarding the importance of considering the horizontal and vertical ownership limits in context with the Commission's prior decisions on rate regulation and program access. Given the existing behavioral regulations imposed on vertically integrated cable operators and programming vendors, I emphasize that these cable ownership provisions will play a critical role in determining whether the future broadband network will ultimately belong to all multichannel competitors, including cable operators, to the extent that they remain able to invest and exercise creativity. Similarly, I will remain interested in the extent to which the channel occupancy rules permit future opportunities for investment and development of new ventures and programming. I am also concerned that these ownership rules--as well as all the implementing regulations for the 1992 Cable Act--incorporate sufficient flexibility to address the unique economic concerns of small operators and minority programmers in order to continue to foster a dynamic industry.

Concerning specific proposals contained in the *Further Notice*,

I will be interested in seeing comment from the public on the merits of the proposed 25% limit on homes passed nationally, or another appropriate standard within the 20-35% range of homes passed. I am also interested in comment regarding the possibility of incorporating a provision for a higher horizontal ownership threshold where systems are minority controlled. With respect to the channel occupancy limits, I am especially interested in comments regarding our proposal to allocate additional channel capacity to vertically integrated programming services that are minority-owned.

Supreme Court, U.S.
FILED
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No. 01-223

In the Supreme Court of the United States

CONSUMER FEDERATION OF AMERICA, ET AL., PETITIONERS

v.

FEDERAL COMMUNICATIONS COMMISSION, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL RESPONDENTS IN OPPOSITION

THEODORE B. OLSON
Solicitor General
Counsel of Record

ROBERT D. MCCALLUM, JR.
Assistant Attorney General

MARK B. STERN
JACOB M. LEWIS
Attorneys

Department of Justice
Washington, D.C. 20530-0001
(202) 514-2217

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QUESTION PRESENTED

Congress has authorized the Federal Communications Commission "to prescribe rules and regulations establishing reasonable limits on the number of cable [television] subscribers a person is authorized to reach through cable systems owned by such person, or in which such person has an attributable interest," 47 U.S.C. 533(f)(1)(A). The question presented is:

Whether a Federal Communications Commission's rule, which limits the number of cable television subscribers that a cable operator may serve to no "more than 30% of all multichannel-video programming subscribers nationwide," 47 C.F.R. 76.503(a), exceeds the Commission's authority under 47 U.S.C. 533(f)(1)(A).

PARTIES TO THE PROCEEDINGS

Petitioners, intervenors below, are the Consumer Federation of America, Consumers Union, Center for Media Education, Association of Independent Video and Filmmakers, National Association of Artists, National Alliance for Media Arts and Culture, Office of Communication of the United Church of Christ, Inc., and National Council of Senior Citizens.

Respondents are Time Warner Entertainment Company, L.P., Bell South Telecommunications, Inc., Bell Atlantic Telephone Companies, AT&T Corporation, Cox Communications, Inc., and U.S. WEST, Inc.

Pursuant to this Court's Rule 12.6, the Federal Communications Commission and the United States of America are also respondents in this Court.

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In the Supreme Court of the United States

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CONSUMER FEDERATION OF AMERICA, ET AL., PETITIONERS

v.

FEDERAL COMMUNICATIONS COMMISSION, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL RESPONDENTS IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (1 Pet. App. 1-29) is reported at 240 F.3d 1126. The rules under review were adopted in *In re Implementation of Sections 11 and 13 of the Cable Television Consumer Protection and Competition Act of 1992, Horizontal and Vertical Ownership Limits*, Second Report and Order, 8 F.C.C.R. 8565 (1 Pet. App. 53-96), *In re Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992, Horizontal Ownership Limits*, Memorandum Opinion and Order on Reconsideration and Further Notice of Proposed Rulemaking, 13 F.C.C.R. 14,462 (1 Pet. App. 114-180), and *In re Implementation of Section 11(c) of the Cable*

Television Consumer Protection and Competition Act of 1992, Horizontal Ownership Limits, Third Report and Order, 14 F.C.C.R. 19,098 (2 Pet. App. 254-311).

JURISDICTION

The court of appeals entered its judgment on March 2, 2001. A petition for rehearing was denied on May 4, 2001 (1 Pet. App. 30-31). The petition for a writ of certiorari was filed on August 2, 2001. This Court's jurisdiction is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. The Cable Television Consumer Protection and Competition Act of 1992 (1992 Cable Act), Pub. L. No. 102-385, 106 Stat. 1460, was the product of "three years of hearings on the structure and operation of the cable television industry." *Turner Broad. Sys., Inc.* v. *FCC*, 512 U.S. 622, 632 (1994). In express legislative findings, Congress found that "the cable television industry ha[d] become a dominant nationwide video medium," with more than "60 percent of the households with televisions" subscribing. 1992 Cable Act § 2(a)(3), 106 Stat. 1460, *reprinted in* 47 U.S.C. 521 note. Congress further determined that, "[f]or a variety of reasons, including local franchising requirements and the extraordinary expense of constructing more than one cable television system to serve a particular geographic area, most cable television subscribers have no opportunity to select between competing cable systems." 1992 Cable Act § 2(a)(2), 106 Stat. 1460. "The result," Congress found, "is undue market power for the cable operator as compared to that of consumers and video programmers." *Ibid.*

Congress also found that the "cable industry has become highly concentrated." 1992 Cable Act § 2(a)(4), 106 Stat. 1460, *reprinted in* 47 U.S.C. 521 note. Con-

gress expressed concern that "[t]he potential effects of such concentration are barriers to entry for new programmers and a reduction in the number of media voices available to consumers." *Ibid.* Accordingly, in the 1992 Cable Act, Congress required the Federal Communications Commission (FCC) "to prescribe rules and regulations establishing reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such person, or in which such person has an attributable interest." 47 U.S.C. 533(f)(1)(A). Congress intended that the subscriber limit provision would decelerate horizontal integration in the cable television industry.

Pursuant to that statutory authorization, the FCC promulgated regulations implementing the 1992 Cable Act's subscriber limits provision. The FCC's regulations provide generally that "no cable operator shall serve more than 30% of all multichannel-video programming subscribers nationwide through multichannel video programming distributors owned by such operator or in which such cable operator holds an attributable interest." 47 C.F.R. 76.503(a).[1]

2. Respondents Time Warner Entertainment Company and AT&T Corporation, two of the nation's larg-

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[1] A "multichannel video programming distributor" is a person "who makes available for purchase, by subscribers or customers, multiple channels of video programming," and includes a "cable operator" as well as a "direct broadcast satellite service." 47 U.S.C. 522(13) (1994 & Supp. V 1999). See also 47 C.F.R. 76.503(e) (parallel definition of "multichannel-video programming subscribers"). An "attributable interest" is defined, by regulation, as including "[a]ctual working control" of an entity, as well as "partnership and direct ownership interests and any voting stock interest amounting to 5% or more of the outstanding voting stock of a corporation." 47 C.F.R. 76.501 nn.1, 2(a)

est cable operators, filed a petition for review challenging the FCC's subscriber limit rule in the United States Court of Appeals for the District of Columbia Circuit. The court of appeals held (1 Pet. App. 1-29) that the FCC's subscriber limit rule was, "[o]n the record before [it], * * * in excess of statutory authority," and remanded the rule to the agency "for further consideration," *id.* at 17, 22.

The court of appeals recognized, as it previously had in upholding the constitutionality of the subscriber limit provision of the underlying statute (see *Time Warner Entertainment Co.* v. *United States*, 211 F.3d 1313, 1319-1320 (D.C. Cir. 2000), cert. denied, 121 S. Ct. 1167 (2001)), that the government's interests in promoting "diversity in ideas and speech" and preserving competition are substantial. 1 Pet. App. 6. The court further held that the FCC was "on solid ground in asserting authority to be sure that no single company could be in a position singlehandedly to deal a programmer a death blow." *Id.* at 8. "If [the] interest in diversity is to mean anything in this context," the appeals court stated, "the government must be able to ensure that a programmer ha[s] at least two conduits through which it can reach the number of viewers needed for viability—independent of concerns over anticompetitive conduct." *Ibid.* The appeals court also "[a]ssum[ed] the validity of the premises supporting the FCC's conclusion" that the average cable programmer needs an "open field" of 40% of the market to be economically viable. *Id.* at 8-9.

The court of appeals, however, rejected (1 Pet. App. 7) as unsubstantiated the FCC's determination that a 30% cap on subscriptions was necessary to ensure that a programmer would have the required open field of 40% of the market in the event that "the two largest cable companies deny carriage, acting 'individually or

collusively.'" The court of appeals found (*id.* at 9-11) no "record support for inferring a non-conjectural risk of collusive rejection." In so holding, the court acknowledged that the 1992 Cable Act "plainly alludes to the *possibility* of collusion when it authorizes regulations to protect against '*joint* actions by a group of operators of sufficient size.'" *Id.* at 9 (citing 47 U.S.C. 533(f)(2)(A) (emphasis added)). But the court held (*ibid.*) that the statutory language is "not itself a congressional finding of actual or probable collusion." The court further acknowledged the "economic commonplace that, all other things being equal, collusion is less likely when there are more firms," but it found that, "by itself," that observation "lends no insight into the question of what the appropriate horizontal limit is," because it "will always be true, although marginally less so for each additional firm." *Id.* at 10.[2]

The court of appeals also stated that "the assessment of a real risk of anti-competitive behavior—collusive or not—is itself dependent on an understanding of market power," and that "normally a company's ability to exercise market power depends not only on its share of the market, but also on the elasticities of supply and demand, which in turn are determined by the *availability*

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[2] The court of appeals did not, however, "foreclose the possibility that there are theories of anti-competitive behavior other than collusion that may be relevant to the horizontal limit and on which the FCC may be able to rely on remand." 1 Pet. App. 11. For example, the court stated, a single cable operator, "acting alone rather than 'jointly,' might perhaps be able to" engage in anti-competitive acts "while serving somewhat less than * * * 60% of the market * * * and the risk might justify a prophylactic limit under the statute." *Ibid.* The court emphasized, however, that "the FCC made no attempt to justify its regulation on these grounds." *Ibid.*

of competition." 1 Pet. App. 12-13. In light of "the substantial changes in the cable industry since publication of the *Third Report* in 1999," the appeals court stated that, "in revisiting the horizontal rules the Commission will have to take account of the impact of DBS [direct broadcast satellite] on that market power." *Id.* at 13.

Finally, the court of appeals rejected the FCC's alternative contention that a 30% limit was necessary to ensure that independent decisions by two large cable companies could not reduce a programmer's open field below the requisite 40% threshold. 1 Pet. App. 13-17. The court emphasized that the statute requires the FCC, in prescribing its implementing rules, "to ensure that no cable operator or group of cable operators can unfairly impede, either because of the size of any individual operator or because of joint actions by a group of operators of sufficient size, the flow of video programming from the video programmer to the consumer." *Id.* at 15 (quoting 47 U.S.C. 533(f)(2)(A)). The court stated that it was unable to "see how the word unfair could plausibly apply to the legitimate, independent editorial choices of multiple [cable operators]." *Ibid.*

In sum, while the court of appeals acknowledged that "[t]he 'interrelated interests' of promoting diversity and fair competition run throughout the 1992 Cable Act's various provisions," 1 Pet. App. 15-16, it held that "Congress's *primary* concern" underlying the subscriber limits "is 'fair' competition," *id.* at 16. The court accordingly adopted a reading of the statute "that sharply confines the authority to regulate solely in the interest of diversity." *Ibid.* Because "the Commission has pointed to nothing in the record supporting a non-conjectural risk of anticompetitive behavior," the court

"reverse[d] and remand[ed] with respect to the 30% rule." *Id.* at 17.[3]

3. In the wake of the court of appeals' decision, the FCC recently initiated a rulemaking to review its subscriber limit rule and to "adopt regulations that are appropriate given the market power of cable operator[s] in today's dynamic and changing MVPD [multichannel video programming distributor] marketplace." *In re Implementation of Section 11 of the Cable Television Consumer Protection and Competition Act of 1992*, Further Notice of Proposed Rulemaking, FCC 01-263, 2001 WL 1104549, para. 44 (Sept. 21, 2001).

ARGUMENT

While we disagree with the court of appeals' judgment and cramped analysis of the FCC's authority to ensure a diversity of views and to promote fair competition in the cable industry, we do not believe that review by this Court is warranted at this time. The court of appeals' decision does not foreclose the FCC's 30% subscriber limit; it simply requires greater record substantiation for the FCC's marketplace assumptions. To that end, the FCC has recently initiated a rulemaking proceeding to review its subscriber limit rules in light of the changes that have occurred in the marketplace since they were first adopted. The pendency

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[3] In addition to the FCC's subscriber limit rule, the court of appeals addressed (1 Pet. App. 17-29) the validity of the agency's channel occupancy and attribution rules (see 47 C.F.R. 76.504(a) (generally prohibiting a cable operator from devoting "more than 40 percent of its activated channels to the carriage of national video programming services owned by the cable operator or in which the cable operator has an attributable interest"); 47 C.F.R. 76.501 nn.1, 2(a) (defining attributable interest)). Petitioners have not sought review of those rulings.

of that rulemaking proceeding would make review by this Court premature and potentially unnecessary.

1. Contrary to the court of appeals' decision (1 Pet. App. 1-17), the subscriber limit rule falls comfortably within the authority vested in the FCC by the 1992 Cable Act. Congress specifically directed the FCC to promulgate subscriber limits on cable operators both to promote a diversity of views and to further fair competition in the information marketplace. See *Time Warner Entertainment Co.* v. *United States*, 211 F.3d 1313, 1319-1320 (D.C. Cir. 2000), cert. denied, 121 S. Ct. 1167 (2001); cf. *Turner Broad. Sys., Inc.* v. *FCC*, 520 U.S. 180, 189 (1997). In particular, the statute requires that the FCC's subscriber limit rule not only "ensure that no cable operator or group of cable operators can unfairly impede, either because of the size of any individual operator or because of joint actions by a group of operators of sufficient size, the flow of video programming from the video programmer to the consumer," 47 U.S.C. 533(f)(2)(A), but also avoid "limitations which would impair the development of diverse and high quality video programming," 47 U.S.C. 533(f)(2)(G).

The statute's findings likewise reflect Congress's dual concerns that the cable industry's highly concentrated market structure could give rise to "barriers to entry for new programmers," as well as "a reduction in the number of media voices available to consumers." 1992 Cable Act § 2(a)(4), 106 Stat. 1460, *reprinted in* 47 U.S.C. 521 note. Indeed, Congress could not have been more clear when it adopted a "Statement of Policy" expressing its desire that the FCC's regulations both "ensure that cable television operators do not have undue market power vis-a-vis video programmers and consumers," and "promote the availability to the public

of a diversity of views and information through cable television and other video distribution media." 1992 Cable Act §§ 2(b)(1), 2(b)(5), 106 Stat. 1463, *reprinted in* 47 U.S.C. 521 note. The FCC's subscriber limit rule directly advances the congressional goals of promoting both diversity and fair competition.

a. By capping subscription levels at 30%, the rule ensures that two large cable operators, either collusively or independently, cannot deny a video programmer access to that 40% of the market that the FCC determined was necessary to launch a viable independent network. The court of appeals nevertheless invalidated the rule on the ground that the FCC had "put forth no evidence at all that indicates the prospects for collusion," even among two dominant cable operators. 1 Pet. App. 11. But the 1992 Cable Act itself expressly anticipates the possibility of collusion among large cable operators: the Act instructs the FCC to protect, through its regulation, against "joint actions by a group of operators of sufficient size." 47 U.S.C. 533(f)(2)(A).

In addition, as the court of appeals acknowledged, it is an "economic commonplace that, all other things being equal, collusion is less likely when there are more firms." 1 Pet. App. 10. See also *FTC* v. *H.J. Heinz Co.*, 246 F.3d 708, 715 (D.C. Cir. 2001) ("Merger law 'rests upon the theory that, where rivals are few, firms will be able to coordinate their behavior, either by overt collusion or implicit understanding.'"). Indeed, to the extent that the court of appeals' opinion may be interpreted as insisting on specific prior evidence of anti-competitive conduct, it would be inconsistent with the court's earlier determination that the subscriber limit is a "structural limitation" that was intended to "add[] a prophylaxis to the law." *Time Warner*, 211 F.3d at 1320. In the end, the court of appeals' decision

pays scant heed to this Court's admonition that the FCC's predictive judgments do not require "complete factual support in the record," and that "a forecast of the direction in which future public interest lies necessarily involves deductions based on the expert knowledge of the agency." *FCC* v. *National Citizens Comm. for Broad.*, 436 U.S. 775, 814 (1978); accord *FCC* v. *WNCN Listeners Guild*, 450 U.S. 582, 594-595 (1981).

b. Furthermore, the court of appeals' decision overlooks that the 1992 Cable Act also was intended to promote a diversity of viewpoints. By ensuring that the two largest cable firms do not have the power to deny a new video programmer access to an economically critical portion of the market, the FCC's subscriber limit rule promotes the viability of new video programmers and thereby advances the government's interest in promoting "diverse * * * video programming." 47 U.S.C. 533(f)(2)(G); see also 1 Pet. App. 14 ("Everything else being equal, each additional 'voice' may be said to enhance diversity."). Thus, even if competitive concerns were alone insufficient to support the FCC's 30% cap, the 1992 Cable Act's interest in promoting diversity, singly or in combination with those competitive concerns, should have sufficed to sustain the rule.

The court of appeals found (1 Pet. App. 14) the promotion of diversity to be an insufficient justification for the rule because, "at some point * * * the marginal value of such an increment in 'diversity' would not qualify as an 'important' governmental interest," such as "moving from 100 possible combinations to 101." That concern about de minimis enhancements in diversity, however, has no relevance here. The FCC's subscriber rule establishes a foundational level of diversity by ensuring that there will be at least four market

participants, no two of which can foreclose long-term entry by an independent programmer, and thus prevents the two largest cable distributors from completely dominating the market. The court's ability to imagine hypothetical situations where the incremental increase in diversity might not justify a regulation thus provides no basis for invalidating a regulation whose actual and foreseeable operation substantially enhances the congressional goal of diversity.

Finally, the court of appeals held (1 Pet. App. 15-17) that the FCC's regulation paid insufficient heed to Congress's concern about "joint" actions by operators that impede competition. See 47 U.S.C. 533(f)(2)(A) (FCC must ensure that "no cable operator or group of cable operators can unfairly impede, either because of the size of any individual operator or because of joint actions by a group of operators of sufficient size, the flow of video programming from the video programmer to the consumer."). But that provision is merely one of seven objectives—including the promotion of diverse programming—that Congress intends the subscriber limit rule to advance. See 47 U.S.C. 533(f)(2)(A)-(G). The court of appeals thus erred in treating Congress's concerns regarding competition as eclipsing other comparably important legislative considerations.

2. Notwithstanding our disagreement with the court of appeals' decision, this Court's review is not warranted at this time. First, the court's decision was limited (1 Pet. App. 17) to "the record before [it]." The decision thus leaves open the possibility that the same or similar regulatory limits will be sustained if the FCC creates a stronger record of an actuality or probability of collusion or other anti-competitive conduct, or offers a more extensive explanation for its assumptions about

marketplace behavior. *Ibid.* Relatedly, the court of appeals did "not foreclose the possibility that there are theories of anti-competitive behavior other than collusion that may be relevant to the horizontal limit and on which the FCC may be able to rely on remand." *Id.* at 11 (suggesting that a single dominant operator might be able to engage in anti-competitive acts against programmers even if it lacked the power to block entry entirely).

Second, as the court of appeals recognized (1 Pet. App. 13), there have been "substantial changes in the cable industry since publication of the *Third Report* in 1999." In its latest report on competition in the video programming marketplace, the FCC found that "[b]etween June 1999 and June 2000, the number of [direct broadcast satellite] subscribers grew from 10.1 million households to almost 13 million households," or "nearly three times the cable subscriber growth rate." *In re Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Seventh Annual Report, FCC 01-1, 2001 WL 12938, para. 8 (Jan. 8, 2001). At the end of that period, direct broadcast satellite subscribers represented 15.4% of all multichannel video programming subscribers. *Ibid.* The impact of direct broadcast satellite growth on the market power of cable operators and other changes in the cable industry have substantial relevance to the FCC's reevaluation of its current subscriber limit rule, and it would be premature for this Court to review the FCC's rule in the absence of a fully developed record regarding the impact of those recent developments on the market power of cable operators.

Third, in response to both the court of appeals' decision and significant changes in the cable marketplace, the FCC recently initiated a rulemaking to review its

subscriber limit rule and to "adopt regulations that are appropriate given the market power of cable operator[s] in today's dynamic and changing MVPD marketplace." *In re Implementation of Section 11 of the Cable Television Consumer Protection and Competition Act of 1992*, Further Notice of Proposed Rulemaking, FCC 01-263, 2001 WL 1104549, para. 44 (Sept. 21, 2001). Among other issues, the Notice of Proposed Rulemaking seeks "comment on market conditions and changes that have taken place since the 1992 [Cable] Act," *id.* para. 7, including "comment on the impact of [direct broadcast satellite's] presence on cable operators' market power," *id.* para. 22. The notice specifically asks for "comment and economic evidence that would support or refute the Commission's earlier conclusions" that underlay its subscriber limit rule and that troubled the court of appeals. *Id.* para. 56. The Notice of Proposed Rulemaking, moreover, requests comments on whether the FCC should add a "safe harbor" provision to the rule, which would suspend the ownership limit "so long as a sufficient level of effective competition was maintained." *Id.* paras. 68, 72; see also 66 Fed. Reg. 51,905, 51,906 (Oct. 11, 2001) (synopsis of further notice of proposed rulemaking).

In light of the pending rulemaking proceeding, review by this Court is not warranted at this time. If the FCC reaffirms the rule essentially in its present form, interested parties will be free to seek judicial review of the rule on the basis of the record generated in the new rulemaking, rather than the earlier, narrower record addressed by the court of appeals' decision. If, on the other hand, the FCC significantly modifies the rule in light of the information gathered during the rulemaking, the challenge to the rule in its current form will likely be mooted.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

THEODORE B. OLSON
Solicitor General
ROBERT D. MCCALLUM, JR.
Assistant Attorney General
MARK B. STERN
JACOB M. LEWIS
Attorneys

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No. 01-223

IN THE
Supreme Court of the United States

CONSUMER FEDERATION OF AMERICA, *et al.*,
Petitioners,

v.

FEDERAL COMMUNICATIONS COMMISSION, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF IN OPPOSITION FOR TIME WARNER ENTERTAINMENT COMPANY, L.P. and AT&T CORP.

DAVID W. CARPENTER
DAVID L. LAWSON
PAUL J. ZIDLICKY
SIDLEY AUSTIN BROWN & WOOD
1501 K Street, N.W.
Washington, D.C. 20005
(202) 736-8000

Counsel for AT&T Corp.

HENK BRANDS
Counsel of Record
KELLOGG, HUBER, HANSEN, TODD & EVANS, P.L.L.C.
1615 M Street, N.W.
Suite 400
Washington, D.C. 20036
(202) 326-7945

ROBERT D. JOFFE
CRAVATH, SWAINE & MOORE
Worldwide Plaza
825 Eighth Avenue
New York, New York 10019
(212) 474-1000

Counsel for Time Warner Entertainment Company, L.P.

November 2, 2001

QUESTION PRESENTED

The Federal Communications Commission ("FCC"), acting pursuant to 47 U.S.C. § 533(f), promulgated a regulation providing that no single firm may own cable systems serving more than 30% of the nation's subscribers.

The question presented is whether the court of appeals properly remanded the matter to the FCC for further consideration where the record lacked support for the key assumptions upon which the agency based the 30% limit.

CORPORATE DISCLOSURE STATEMENTS

Pursuant to Rule 29.6 of the Rules of this Court, respondents Time Warner Entertainment Company, L.P., and AT&T Corp. state as follows:

Time Warner Entertainment Company, L.P., is a Delaware limited partnership. The general partners in Time Warner Entertainment Company, L.P., each are directly or indirectly wholly owned by AOL Time Warner Inc., a publicly held company. An ownership interest of more than 10% in Time Warner Entertainment Company, L.P., is directly or indirectly held by AT&T Corp., a publicly held company.

AT&T Corp. has no parent company. No publicly held company owns more than 10% of AT&T Corp.'s stock.

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IN THE

Supreme Court of the United States

No. 01-223

CONSUMER FEDERATION OF AMERICA, *et al.*,
Petitioners,

v.

FEDERAL COMMUNICATIONS COMMISSION, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF IN OPPOSITION FOR TIME WARNER ENTERTAINMENT COMPANY, L.P. and AT&T CORP.

Petitioners seek review of a decision of the United States Court of Appeals for the District of Columbia Circuit setting aside an order of the Federal Communications Commission ("FCC") adopting a regulation prohibiting any single firm from owning cable systems serving more than 30% of subscribers nationally. The court of appeals held that the order was insufficiently reasoned and unsupported by the administrative record. Accordingly, the court of appeals remanded the case for further consideration.

Petitioners point to no special circumstances warranting further review. There is no conflict of authority, and the decision below is not of such broad significance as to merit review in the absence of a conflict. The court of appeals did not hold that the FCC may not adopt any subscriber limit. Because the FCC is currently attempting to address the deficiencies in a rulemaking on remand, the practical

significance of the decision below is limited. Moreover, the court of appeals did not announce any new principles: petitioners' quarrel is solely with the application of settled law. In light of these considerations, it is not surprising that the FCC itself has declined to seek review: only interest groups that intervened below have petitioned. It would be extraordinary for this Court to grant certiorari where review is not sought by, and is unwarranted in the view of, the agency directly affected.

Moreover, the decision of the court of appeals is correct. As the court of appeals concluded, a crucial step in the FCC's reasoning — that cable operators are likely to collude in denying carriage to new video programming services — is without any record support. The court of appeals was also correct in holding that the FCC's alternative rationale (if there was one) fails. That rationale — that a 30% limit is justified because splintering the nation's cable operators promotes a diversity of viewpoints — is entirely unhelpful in justifying any particular percentage limit. Besides, the court of appeals was plainly right in determining that the statute at hand, 47 U.S.C. § 533(f), does not permit reliance on this rationale.

Accordingly, the petition should be denied.

STATEMENT

1. In 1992, Congress enacted the Cable Television Consumer Protection and Competition Act, Pub. L. No. 102-385, 106 Stat. 1460. The so-called subscriber-limits provision of that statute provides: "In order to enhance effective competition, the Commission shall . . . prescribe rules and regulations establishing reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such person." 47 U.S.C. § 533(f)(1)(A). The statute further provides that, "[i]n prescribing rules and regulations . . . , the Commission shall, among other public

interest objectives[,] . . . ensure that no cable operator or group of cable operators can unfairly impede, either because of the size of any individual operator or because of joint actions by a group of operators of sufficient size, the flow of video programming from the video programmer to the consumer." *Id.* § 533(f)(2)(A).

In the ensuing rulemaking, the FCC promulgated a regulation prohibiting any single firm from owning cable systems passing more than 30% of the total number of homes passed by cable systems nationally. *See Implementation of Sections 11 and 13 of the Cable Television Consumer Protection and Competition Act of 1992; Horizontal and Vertical Ownership Limits*, Second Report and Order, 8 FCC Rcd 8565 (1993) (Pet. App. 53). According to the FCC, such a rule was necessary to prevent "the possibility that large horizontally integrated MSOs [Multiple System Operators — *i.e.*, cable companies owning multiple cable systems] might have the ability to preclude the launch of new video programming services." Pet. App. 66. The FCC did not explain, however, why that rationale implied a 30% limit, stating only that drawing the line at 30% reasonably balanced the stated concern against "the benefits and efficiencies that result from greater horizontal concentration." *Id.*[1]

Respondent Time Warner filed a petition for review in the D.C. Circuit. While that petition was pending, however, the FCC reopened its rulemaking. *See Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992; Horizontal Ownership Limits*,

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[1] The FCC stayed the effectiveness of its rule while the constitutionality of the statute was being litigated. *See* Pet. App. 92. The rule did not become effective until May 19, 2000, *see Cable Television Consumer Protection and Competition Act of 1992; Horizontal Ownership Limits*, 65 Fed. Reg. 36382 (June 8, 2000), and had been in effect for less than one year when it was set aside by the decision below.

Memorandum Opinion and Order on Reconsideration and Further Notice of Proposed Rulemaking, 13 FCC Rcd 14462 (1998) (Pet. App. 114). In October 1999 (after Time Warner filed its briefs explaining the shortcomings of the FCC's reasoning, but before the court of appeals could hear argument), the FCC issued a new order. *See Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992; Horizontal Ownership Limits*, Third Report and Order, 14 FCC Rcd 19098 (1999) (Pet. App. 254). In that order, the FCC reaffirmed the 30% cap.

For the first time, however, the FCC's October 1999 order sought to link the 30% line drawn to the previously expressed rationale — namely, that large cable companies might impede entry by new video programming services. The agency did so through the following chain of reasoning. *First*, the FCC estimated that a new video programming network "needs 15 million subscribers in order to have a reasonable chance to achieve economic viability." Pet. App. 283. The FCC calculated that 15 million subscribers represented about 20% of the total subscriber universe. *See id.* at 284. *Second*, the FCC estimated that, on average, a new video programming service would have only about a 50% success rate in gaining carriage even if cable operators did not act anticompetitively. *See id.* at 288. Based on these two steps, the FCC concluded that, to be viable, a new video programming service would need an "open field" of 40%. *Id.* at 289.

To the two steps described above, which still justified a cap no lower than 60%, the FCC then added a crucial third step. The FCC concluded that it should ensure new video programming services access to the requisite open field even if the two largest cable companies were to deny carriage "collusively." *Id.* at 290. Although the FCC did not point to any evidence that cable companies had ever colluded in denying carriage, it suggested that Congress itself had found collusive denial of

carriage to be a realistic threat. *See id.* at 284, 289. Moreover, the FCC said, the existence of this threat was an "assumption" that was "not unreasonable": cable operators that are "vertically integrated" might have "incentives" both "to reach carriage decisions beneficial to each other" and "to encourage one another to carry the same non-vertically integrated programming in order to share the costs of such programming." *Id.* at 284-85. And, the agency said, "[t]he probability of tacit collusion is higher with 2 competitors than 3 competitors." *Id.* at 289.

Thus, the FCC again settled on a 30% cap, which would yield a 40% open field even if the top two cable companies colluded in denying cable carriage. *Id.* The agency further noted that the 30% choice also had the consequence of "ensuring that there will be at least 4 MSOs in the marketplace." *Id.* at 290. That consequence was a "salutary" one, the FCC said, because, "[w]ith more MSOs making purchasing decisions," there would be an "increase[d] . . . likelihood that the MSOs will make different programming choices and a greater variety of media voices will therefore be available to the public." *Id.*

2. Respondents Time Warner and AT&T filed petitions for review of the October 1999 order in the D.C. Circuit, asserting that the FCC's choice of a 30% cap was inconsistent with the First Amendment, as well as the Administrative Procedure Act ("APA") and the subscriber-limits provision itself. *See* Pet. App. 2. In their brief, the FCC and the United States conceded that intermediate First Amendment scrutiny applied, *see* Brief for Respondents at 15-16, *Time Warner Entertainment Co. v. FCC*, No. 94-1035 (and consolidated cases) (D.C. Cir. filed Apr. 6, 2000) ("FCC Br."), but argued that the 30% limit could survive such scrutiny, *see id.* at 30-32. Petitioners in this Court (various interest groups) intervened in the court of appeals but did not file a merits

brief. Instead, petitioners filed a motion for leave to "adopt" the brief filed by the FCC and the United States.[2]

By a unanimous vote, the court of appeals set aside the FCC's subscriber-limits rule. *See* Pet. App. 1-29.[3] Applying the familiar standard for intermediate First Amendment scrutiny of *United States v. O'Brien*, 391 U.S. 367 (1968), and this Court's *Turner* decisions,[4] the court held that the FCC was required to show that the subscriber limit "advances important governmental interests unrelated to the suppression of free speech and does not burden substantially more speech than necessary to further those interests." Pet. App. 5-6 (internal quotation marks omitted). This meant that the FCC would have to "'demonstrat[e] that the recited harms are real, not merely conjectural,'" *id.* at 6 (quoting *Turner I*, 512 U.S. at 664 (plurality opinion)), through "'reasonable inferences based on substantial evidence,'" *id.* at 10 (quoting *Turner I*, 512 U.S. at 666 (plurality opinion)).

The court of appeals acknowledged that, in a previous decision, it had rejected a facial First Amendment challenge to the *statute*, holding that the subscriber-limits statute was sufficiently tailored to "'the promotion of diversity in ideas and speech' and 'the preservation of competition.'" *Id.* at 6

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[2] *See* Motion of Center for Media Education, *et al.*, To Adopt Government's Brief, *Time Warner Entertainment Co. v. FCC*, No. 94-1035 (and consolidated cases) (D.C. Cir. filed Apr. 13, 2000). The motion was granted a few days later. *See* Order, *Time Warner Entertainment Co. v. FCC*, No. 94-1035 (and consolidated cases) (D.C. Cir. Apr. 18, 2000).

[3] The court of appeals also reviewed challenges to two other sets of FCC rules: the so-called channel-occupancy and attribution rules. *See* Pet. App. 17-22, 22-29. Petitioners do not challenge the court of appeals' rulings in connection with those rules.

[4] *Turner Broadcasting System, Inc. v. FCC*, 512 U.S. 622 (1994) ("*Turner I*"); *Turner Broadcasting System, Inc. v. FCC*, 520 U.S. 180 (1997) ("*Turner II*").

(quoting *Time Warner Entertainment Co. v. United States*, 211 F.3d 1313, 1319 (D.C. Cir. 2000), *cert. denied*, 121 S. Ct. 1167 (2001)). But, the court held, "[c]onstitutional authority to impose some limit is not authority to impose any limit imaginable." *Id.* at 5. In particular, "the FCC must still justify the limits that it has chosen as not burdening substantially more speech than necessary. In addition, in 'demonstrat[ing] that the recited harms are real, not merely conjectural,' . . . the FCC must show a record that validates the *regulations*, not just the abstract statutory authority." *Id.* at 6 (quoting *Turner I*, 512 U.S. at 664 (plurality opinion)).

Applying these principles, the court of appeals determined that the FCC's decision to draw the line at 30% was unsubstantiated. The court assumed for purposes of its analysis the validity of the first two steps in the FCC's reasoning: that a new video programming service needs 20% of subscribers to be viable and that, given an average success rate of 50%, the service needs an "open field" of 40%. *See id.* at 7, 8-9. But those two steps alone, the court observed, could justify a cap no lower than 60%. *Id.* at 9. The FCC's selection of a 30% cap thus crucially depended on the third step in the FCC's reasoning: that two cable companies might act in concert to refuse to carry new programming services. *Id.* Again for purposes of discussion, the court assumed that this third step could lawfully support a 30% limit if the administrative record before the FCC demonstrated a non-conjectural risk of collusion. *See id.* at 8.

But the court of appeals found that there was no "record support for inferring a non-conjectural risk of collusive rejection." *Id.* at 9. At the outset, the court noted, the FCC could not rely on Congress to substantiate the risk of collusion: although the statute plainly authorized the FCC to act if, upon inquiry, it determined that collusion was a realistic problem, Congress had not made a finding that such

a risk existed. *See id.* And the court determined that, to the extent the FCC had made its own finding of likely collusion, that finding was unsubstantiated and unexplained. *See id.* at 10. As the court noted, the FCC never explained why vertical integration would result in collusion — a failure that was particularly troubling because the FCC had not pointed to a single real-world example of collusive denial of carriage. *See id.* Moreover, the FCC's reliance on "the economic commonplace that, all other things being equal, collusion is less likely when there are more firms" casts no light at all on "the question of what the appropriate horizontal limit is." *Id.*

Thus, the court of appeals concluded that the third step in the FCC's reasoning simply could not pass muster under the applicable level of scrutiny. Although the court acknowledged that "[s]ubstantial evidence does not require a complete factual record," *id.*, it found that "the FCC ha[d] put forth no evidence at all that indicates the prospects for collusion," *id.* at 11; *see also id.* at 17 ("the Commission has pointed to nothing in the record supporting a non-conjectural risk of . . . collusion").

The court of appeals next suggested that the FCC might have relied on an alternative justification: that, even if no risk of collusion existed, giving programming services at least four carriage opportunities would promote the interest of making available a diversity of voices. *See id.* at 13 (quoting the FCC's statement that a 30% cap would "serv[e] the salutary purpose of ensuring that there will be at least 4 MSOs in the marketplace"). But, the court concluded, this "more is better" diversity rationale was problematic in its own way.

As the court of appeals explained, "regulat[ing] the coincidental but independent actions of cable operators solely in the interest of diversity" might raise serious First Amendment concerns. *Id.* at 7. For one thing, any interest in splintering

cable operators to this end at some point could no longer "qualify as an 'important' governmental interest." *Id.* at 14. For another thing, "it would be odd to discover that although a newspaper that is the only general daily in a metropolitan area cannot be subjected to a right of reply, *see Miami Herald Publishing Co. v. Tornillo*, 418 U.S. 241 (1974), it could in the name of diversity be forced to self-divide." *Id.* But, the court determined, "[w]e need not face [this First Amendment] issue." *Id.* "[U]sing traditional tools of statutory interpretation," the court concluded, "Congress has not given the Commission authority to impose [a subscriber limit] solely on the basis of the 'diversity' precept." *Id.*

Carefully analyzing "[t]he relevant section," Section 533(f)(2)(A), the court of appeals noted that this provision instructed the FCC to address "only 'unfair[]' impediments to the flow of programming." *Id.* at 14-15 (brackets in original). The court concluded that "we cannot see how the word unfair could plausibly apply to the legitimate, independent editorial choices of multiple [cable companies]." *Id.* at 15. Moreover, the court explained, the FCC's reading "effectively deletes the word 'joint'" from the statutory phrase "because of joint actions by a group of operators." *Id.* Finally, the court noted, the sole purpose expressed in the statute was that stated in Section 533(f)(1): "to enhance effective competition." *See id.* at 16. Thus, the court concluded, the 30% limit simply could not be supported on a bare diversity rationale. *Id.* at 17.

For the first time participating on the merits, petitioners filed a petition for rehearing en banc, which was denied. *See id.* at 30-31. The instant petition for a writ of certiorari followed.

REASONS TO DENY THE WRIT

I. THE PETITION POINTS TO NO CIRCUMSTANCES WARRANTING FURTHER REVIEW.

Petitioners do not assert that the decision of the court of appeals conflicts with that of any other court of appeals, and they could not: there simply is no conflicting authority. To cushion the impact of this deficiency, petitioners suggest that, because the D.C. Circuit has "exclusive jurisdiction of many telecommunications cases," this Court could not expect there to be a conflict. Pet. 13 n.10; *see also* Pet. 15 n.13, 16 n.14. But the D.C. Circuit has exclusive jurisdiction with respect to only a small subset of communications cases, limited mostly to licensing-related appeals. *See* 47 U.S.C. § 402(b). All other FCC decisions, including rulemaking decisions like that here under review, can be appealed to any court of appeals. *See id.* § 402(a); 28 U.S.C. § 2343. Indeed, many of the most important communications decisions have come from circuits other than the D.C. Circuit.[5]

In the absence of a conflict of authority, certiorari would be appropriate only if there were extraordinarily compelling circumstances. *See* Sup. Ct. R. 10(a). There are none. Contrary to petitioners' implications, the court of appeals did not strike down any statute as unconstitutional and did not hold that the FCC may not adopt a subscriber-limits rule. Instead, the court of appeals held only that the record did not substantiate the 30% cap. The court remanded the matter for further consideration by the FCC, which, six weeks ago,

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[5] *See, e.g., Iowa Utils. Bd. v. FCC*, 219 F.3d 744 (8th Cir. 2000), *cert. granted in part sub nom. Verizon Communications Inc. v. FCC*, 121 S. Ct. 877-79 (2001) (Nos. 00-511, 00-555, 00-587, 00-590 & 00-602); *Schurz Communications, Inc. v. FCC*, 982 F.2d 1043 (7th Cir. 1992); *California v. FCC*, 905 F.2d 1217 (9th Cir. 1990).

issued a notice of proposed rulemaking to that end.[6] Thus, the practical significance of the court of appeals' decision is limited at this time.

Additional review is further inappropriate because the court of appeals, far from announcing any new law, merely applied settled principles. In particular, the court subjected the FCC's reasoning to well-established principles of intermediate First Amendment scrutiny that the FCC itself acknowledged were controlling. These principles have long required agencies to demonstrate that speech-burdening rules are a narrowly tailored response to a real, non-conjectural problem shown to exist by substantial evidence. *See generally Turner I*, 512 U.S. at 666 (plurality opinion). Indeed, petitioners concede as much: they assert that the court of appeals applied First Amendment scrutiny that was "intermediate in theory, but strict in fact," Pet. 23, 29-30, thereby confirming that their quarrel is with the application of the "non-conjectural harm"/"substantial evidence" standard to the administrative record — not with the formulation of any legal principle. But, as this Court has held, "[t]he responsibility to assess the record to determine whether agency findings are supported by substantial evidence is not ours," but "primarily the task of the courts of appeals." *Mobil Oil Corp. v. FPC*, 417 U.S. 283, 309 (1974); *see generally* Robert Stern, Eugene Gressman,

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[6] *See Implementation of Section 11 of the Cable Television Consumer Protection and Competition Act of 1992*, Further Notice of Proposed Rulemaking, CS Docket No. 98-82, *et al.*, FCC 01-263, 2001 WL 1104549, ¶¶ 1, 7 (rel. Sept. 21, 2001) ("In *Time Warner Entertainment Co. v. FCC* [240 F.3d 1126 (D.C. Cir. 2001)], the United States Court of Appeals for the D.C. Circuit reviewed the Commission's cable television horizontal and vertical ownership limits and attribution benchmarks, and reversed and remanded the rules. . . . In accordance with our statutory mandate, First Amendment principles, and the . . . *Time Warner* decision, we now seek to reexamine our rules . . . .") (footnotes omitted).

Stephen Shapiro & Kenneth Geller, *Supreme Court Practice* 189 (7th ed. 1993) ("Stern & Gressman").

Petitioners nevertheless try to infuse the court of appeals' decision with broad significance by predicting that it will "bring immediate and sweeping changes to ownership concentration in *all* electronic media industries." Pet. 13. But most of the examples to which petitioners point consist of nothing more than instances in which courts granted preliminary relief or in which private parties made arguments in briefs or elsewhere. *See* Pet. 14-16. Besides, even if any ownership rules were in danger, that would be because those rules as currently framed cannot satisfy settled principles of intermediate First Amendment scrutiny — not because of any legal principle that the court of appeals announced for the first time in the decision below.

In light of the considerations set forth above, it is not surprising that the actual parties that suffered defeat below, the FCC and the United States, have declined to seek certiorari. If the expert agency charged with administering subscriber limits has determined that the court of appeals' decision does not undermine its programmatic objectives to such an extent as to warrant further review, then there is no cause for this Court to conclude otherwise.

II. THE COURT OF APPEALS' DECISION IS CORRECT.

The court of appeals not only applied settled principles of law to the record before it, but also did this correctly. The court of appeals correctly determined (and petitioners do not contest) that the FCC's attempt to justify a 30% cap (rather than a 60% cap) depended crucially on the FCC's finding that there was a risk of collusion. The court of appeals also correctly determined (and petitioners again do not contest) that the FCC was therefore required to demonstrate that, based on

reasonable inferences drawn from substantial evidence, the supposed collusion risk was real and not merely conjectural. Thus, petitioners' main quarrel with the court of appeals relates to the court's conclusion that the record facts to which the FCC pointed did not justify a finding of a realistic collusion risk.

Even ignoring that this fact-bound conclusion should be of no interest to this Court, it was unquestionably correct. The FCC pointed to *nothing* in the record to substantiate any likelihood of collusion. The agency did not identify a single real-world example of the kind of collusion that it supposedly feared: an agreement between cable firms not to provide cable carriage to a particular video programming service. Instead, the agency appeared to believe that there was no need for it to make any finding of a realistic collusion risk — on the mistaken theory that Congress had already made that finding for it. And the agency's own speculations were unsupported. The FCC's statement that vertical integration somehow breeds collusion was unexplained and is entirely unsupported by economic theory. And the FCC's reliance on the truism that collusion becomes more likely where there are fewer firms neither supported any finding that collusion of the particular kind feared posed a realistic threat nor helped explain at what level of concentration the threat would become intolerable.

Petitioners are simply wrong when they argue that the court of appeals' decision "conflicts" with decisions of this Court holding that, when an agency's factual determinations are of a "'judgmental or predictive nature,'" there is no need for "'complete factual support in the record.'" Pet. 25 (quoting *FCC v. National Citizens Comm. for Broadcasting*, 436 U.S. 775, 813-14 (1978) ("*NCCB*")). The court of appeals expressly noted that "[s]ubstantial evidence does not require a complete factual record — we must give appropriate deference to predictive judgments that necessarily involve the

expertise and experience of the agency." Pet. App. 10 (citing *Turner II*, 520 U.S. at 196; *NCCB*, 436 U.S. at 814); *see also id.* at 9 ("[w]e give deference to the predictive judgments of Congress, see *Turner II*, 520 U.S. at 195-96 (citing *Turner I*, 512 U.S. at 665)"); *id.* at 27 ("given . . . the inevitable difficulty in picking . . . a number, and the deference due the Commission, we cannot find the choice of 33% arbitrary"). Thus, the "conflict" seen by petitioners could at most be implicit, which by itself disqualifies it from being a credible candidate for review. *See* Stern & Gressman 174.

In any event, there is no conflict, for the court of appeals' application of the intermediate scrutiny standard was entirely correct. Judicial deference to administrative agencies' predictive judgments is not unlimited. Even when reviewing predictive judgments of Congress — which are entitled to greater weight than those of agencies, *see Turner I*, 512 U.S. at 666 (plurality opinion) — courts have an independent obligation of review. As this Court stated in *Turner I*:

> That Congress' predictive judgments are entitled to substantial deference does not mean . . . that they are insulated from meaningful judicial review altogether. On the contrary, we have stressed in First Amendment cases that the deference afforded to legislative findings does "not foreclose our independent judgment of the facts bearing on an issue of constitutional law."

Id. (quoting *Sable Communications of California, Inc. v. FCC*, 492 U.S. 115, 129 (1989)). Courts therefore must ensure that there are "reasonable inferences based on substantial evidence." *Id.* The court of appeals correctly determined that the FCC's predictions did not meet this test: the FCC's "predictive judgment" was based on "*no evidence at all.*" Pet. App. 11 (emphasis added).

Petitioners also wrongly argue that the court of appeals erred in holding that the FCC could not attempt to justify its 30% cap on the basis of a purely diversity-based rationale. At the outset, it is questionable whether the FCC even embraced such a rationale. The closest the FCC's order came to doing so was to say that "the 30% limit serves the salutary purpose of ensuring that there will be at least 4 MSOs in the marketplace," which the agency thought would "increas[e] the likelihood that the MSOs will make different programming choices and a greater variety of media voices will therefore be available to the public." *Id.* at 290. But that statement by its terms was no attempt to justify drawing the line *at 30%*. Indeed, the FCC's brief in the court of appeals never argued that drawing the line at 30% could be justified on a rationale independent from the agency's three-step competition-based rationale. Although the FCC's brief did point to the "at least 4 MSOs in the marketplace" passage in the order, it did so only in support of an argument that there should be *some* cap. *See* FCC Br. 32.

That the FCC did not rely on "programming diversity" to justify its choice of 30% as the appropriate limit is not surprising. As the court of appeals elsewhere noted, diversity considerations alone, although possibly helpful in justifying the proposition that there should be *some* subscriber limit, are entirely unhelpful in justifying a particular percentage line drawn in the face of intermediate scrutiny or even APA review. *See* Pet. App. 18 (FCC must explain "the conditions that make 50% too high and 30% too low"). For example, even if the FCC might cogently state that a diversity objective is served if there are "at least 4 MSOs in the marketplace," that does nothing to explain why the line should be drawn at four, and not at three or five.

In any event, the court of appeals correctly held that the FCC lacks statutory authority to regulate on the basis of a

bare "more is better" rationale. To the extent the FCC rested its cap on a diversity-based rationale at all, it did so in reliance on Section 533(f)(2)(A). *See id.* at 6, 14-15, 284. But that provision directs the FCC only to "ensure that no cable operator or group of cable operators can *unfairly* impede, either because of the size of any individual operator or because of *joint* actions by a group of operators of sufficient size, the flow of video programming from the video programmer to the consumer." 47 U.S.C. § 533(f)(2)(A) (emphases added). As the court of appeals correctly explained, a pure "more is better" rationale would read the terms "unfairly" and "joint" out of the statute. Pet. App. 15. Moreover, while the statute expressly mentions the purpose of "enhanc[ing] effective competition," 47 U.S.C. § 533(f)(1), it says nothing about any purpose of promoting diversity for its own sake. *See* Pet. App. 16.

Petitioners, in contrast, point to language in the lead-in sentence of Section 533(f)(2), which says that the FCC must pursue the listed objectives "among other public interest objectives." Pet. 18, 20. According to petitioners, "[t]his Court has consistently construed the term 'public interest' as embodying diversity." Pet. 18. At the outset, the FCC in its court of appeals brief never argued that this language authorized the agency to adopt a cap on a purely diversity-based rationale. Petitioners, which filed no merits brief, did not so argue until their petition for rehearing,[7] where it came too late.[8] Besides, petitioners do not explain how an indirect

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[7] *See* Petition of Intervenors Consumer Federation of America, *et al.*, for Rehearing or Rehearing *En Banc* at 5, *Time Warner Entertainment Co. v. FCC*, No. 94-1035 (and consolidated cases) (D.C. Cir. filed Apr. 16, 2001).

[8] *See, e.g., Hartford Underwriters Ins. Co. v. Union Planters Bank, N.A.*, 530 U.S. 1, 6 n.2 (2000) ("The Eighth Circuit declined to address this issue, since it had not been raised until the rehearing en banc . . . .

and implicit allusion of this kind can be enough where, as the court of appeals explained, the balance of Section 533(f) strongly militates against this reading.[9]

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

DAVID W. CARPENTER
DAVID L. LAWSON
PAUL J. ZIDLICKY
SIDLEY AUSTIN BROWN & WOOD
1501 K Street, N.W.
Washington, D.C. 20005
(202) 736-8000

Counsel for AT&T Corp.

HENK BRANDS
Counsel of Record
KELLOGG, HUBER, HANSEN, TODD & EVANS, P.L.L.C.
1615 M Street, N.W.
Suite 400
Washington, D.C. 20036
(202) 326-7945

ROBERT D. JOFFE
CRAVATH, SWAINE & MOORE
Worldwide Plaza
825 Eighth Avenue
New York, New York 10019
(212) 474-1000

Counsel for Time Warner Entertainment Company, L.P.

November 2, 2001

We similarly do not reach the issue here.").

[9] Petitioners also point to Sections 533(f)(2)(B), (C), and (G), *see* Pet. 19, but fail to explain how those subsections support their view. In any event, the FCC did not rely on these provisions in its brief below.

No. 01-223

NOV 2 2001

IN THE

Supreme Court of the United States

CONSUMER FEDERATION OF AMERICA, *et al.*,
Petitioners,

v.

FEDERAL COMMUNICATIONS COMMISSION, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF THE NATIONAL ASSOCIATION OF BROADCASTERS AS *AMICUS CURIAE* IN SUPPORT OF CONSUMER FEDERATION OF AMERICA, *ET AL.*

HENRY L. BAUMANN
JACK N. GOODMAN *
JERIANNE TIMMERMAN
NATIONAL ASSOCIATION OF BROADCASTERS
1771 N Street, N.W.
Washington, D.C. 20036
(202) 429-5430

* Counsel of Record

November 2, 2001

WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D. C. 20001

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The National Association of Broadcasters, with consents of the parties, submits this brief *amicus curiae* in support of the Consumer Federation of America, *et al.* (CFA), Petitioners in the above-captioned proceeding.

INTERESTS OF *AMICUS* [1]

The National Association of Broadcasters (NAB) is a nonprofit, incorporated association of radio and television broadcast stations and networks. NAB serves and represents the American broadcasting industry.

This case presents two issues of critical concern to *amicus* and its members. The court of appeals invalidated certain Federal Communication Commission (FCC or Commission) regulations applicable to operators of cable television systems on the grounds that, *inter alia*, the FCC had not met its burden of justifying these regulations under the First Amendment. Broadcast television stations compete with cable systems in the provision of video programming to the public and in the sale of advertising, as well as being the source of the most popular programming on cable systems. The environment in which broadcast stations and cable systems compete has largely been defined by regulations, statutory and administrative. *Amicus*, therefore, is heavily involved in legislative, regulatory and judicial proceedings concerning the regulation of cable television and the video marketplace. Often, cable operators' First Amendment status has been a significant issue in these proceedings, and *amicus* therefore has a vital interest in decisions affecting the nature and scope of the protection afforded cable television systems by the First Amendment.

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[1] Pursuant to S. Ct. R. 37.6, no counsel for a party authored this brief in whole or in part, and no person or entity, other than *amicus*, its members and its counsel, contributed monetarily to the preparation or submission of this brief.

The broadcast stations that are members of NAB also have their vital interests affected, on a daily basis, by regulations promulgated by the FCC pursuant to both (1) its general statutory authority under the Communications Act of 1934 to regulate interstate communications in the "public interest, convenience and necessity," and (2) more specific congressional directives to prescribe rules pertaining to particular subjects or issues. *Amicus* accordingly is concerned about the level of deference that statutory provisions, and FCC regulations adopted pursuant to those provisions, receive from reviewing courts.

SUMMARY OF ARGUMENT

The Court should grant certiorari in this case to address recurring, unresolved questions concerning the appropriate level of First Amendment review of structural economic regulations that affect the cable television industry, or communications industries generally, but that do not directly regulate speech itself. The cable industry has consistently argued to reviewing courts that virtually any type of economic regulations affecting it (such as the ownership rules at issue here) entail serious First Amendment implications and must be subjected to significantly heightened judicial scrutiny. By acquiescing in the cable industry's position, the courts of appeals have failed to consider the practical, legal and policy implications of reflexively subjecting economic regulations to raised constitutional scrutiny.

As will be shown, the heightened scrutiny approach increasingly employed by the courts of appeals is in considerable tension, if not outright conflict, with this Court's decisions. This Court has made clear that the First Amendment should not be read as requiring a heightened level of review for an economic-oriented regulation merely because it affects a communications industry, unless such a regulation was adopted for a speech-repressive or other invidious purpose. *See Leathers v. Medlock*, 499 U.S. 439 (1991).

Although *Turner Broadcasting System, Inc. v. FCC*, 512 U.S. 622 (1994), applied "intermediate" scrutiny to the must carry rules, those rules directly impact the speech of cable operators by requiring them to carry specific broadcast signals, and thus pose a far different question from the one addressed by the court of appeals in this case. Even following *Turner*, members of this Court expressed clear reservations about applying heightened First Amendment scrutiny to the economic regulation of a communications-related industry in oral argument in cases (subsequently mooted by legislation), which involved restrictions on telephone companies providing video programming to subscribers.

This Court should also grant certiorari to clarify the level of deference reviewing courts should give to legislative rules adopted by the FCC pursuant to Congress' express delegation of authority. The lack of deference shown by the court of appeals in this case frustrates the ability of Congress to rely on the experience and expertise of administrative agencies. Furthermore, reviewing courts should not—as this case demonstrates—be able to circumvent the deference owed to Congress by initially rejecting challenges to a statute under deferential review, but then showing virtually no deference to the regulations promulgated by the agency expressly directed by Congress to implement the statute.

REASONS FOR GRANTING REVIEW

I. ECONOMIC REGULATION OF A COMMUNICATIONS-RELATED INDUSTRY SHOULD NOT AUTOMATICALLY RECEIVE HEIGHTENED FIRST AMENDMENT SCRUTINY.

A. The Cable Industry Has Consistently Argued To Reviewing Courts That Virtually Any Economic Regulation Of It Entails Serious First Amendment Concerns.

The decision of the court of appeals in this case to apply heightened First Amendment scrutiny to structural economic

regulation of the cable television industry is indicative of a trend. The cable industry has a long history of contending that any economic-oriented regulation, or regulation affecting its structure, has serious First Amendment implications and must therefore be subjected to significantly heightened judicial scrutiny. For example, the cable industry challenged, on First Amendment grounds, the regulation of the rates it charged consumers because "regulating cable rates inevitably affects both the content and quantity of speech by limiting the amount of money that a cable operator can spend on programming." *Time Warner Entertainment Co., L.P. v. FCC*, 93 F.3d 957, 966 (D.C. Cir. 1996).[2] Although the courts reviewing challenges to economic regulations, such as rate regulation, have on occasion expressed skepticism about certain of the cable industry's claims, the courts have nonetheless increasingly subjected these types of economic or structural regulations to heightened First Amendment scrutiny.[3] The court of appeals in this proceeding similarly

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[2] In that case, the cable industry also claimed that numerous other provisions of the Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460 (1992 Cable Act) and the Cable Communications Policy Act of 1984, Pub. L. No. 98-549, 98 Stat. 2779 (1984 Cable Act) violated the First Amendment, including provisions specifically applicable to vertically integrated video programmers (*i.e.*, video programmers in which cable operators have an ownership interest). The parties challenging these various statutory provisions urged the court to apply strict scrutiny, the most stringent level of First Amendment review under which the government must establish a compelling interest, directly advanced by the least restrictive regulatory means. *See Time Warner,* 93 F.3d at 962, 966.

[3] For instance, when reviewing the FCC's rate regulation rules, the D.C. Circuit "assume[d] that rules requiring cable operators to charge reasonable rates burden speech, *although it is by no means clear how they do so.*" *Time Warner Entertainment Co., L.P. v. FCC*, 56 F.3d 151, 185 (D.C. Cir. 1995) (emphasis added). Despite this apparent reservation, the D.C. Circuit still applied intermediate scrutiny to the FCC's cable rate rules, *id.* at 186, and to the various statutory provisions authorizing rate and other Commission regulation of the cable industry. *See Time Warner*,

applied intermediate scrutiny to the Commission's rules implementing the horizontal and vertical ownership limits of the 1992 Cable Act. *Time Warner Entertainment Co., L.P. v. FCC*, 240 F.3d 1126 (D.C. Cir. 2001) (App. 1-29).[4] Thus, the courts of appeals have, with relatively little consideration in some cases, accepted arguments by the cable and other communications-related industries that structural or other economic regulation of those industries automatically merits a raised level of judicial scrutiny under the First Amendment.[5]

B. The Trend In The Courts Of Appeals To Apply Heightened First Amendment Scrutiny To Structural Economic Regulation Of Media Entities Represents An Unwarranted Extension Of This Court's Precedents.

This Court should grant review in this case to clarify that structural economic regulation is not subject to heightened First Amendment review whenever such regulation is directed at a media or communications entity. Courts of appeals that have accepted the cable industry's arguments

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93 F.3d at 967. For these rate and other regulations to be upheld, the government accordingly had to establish that they advanced substantial governmental interests and did not burden substantially more speech than necessary to achieve those interests. *See Ward v. Rock Against Racism*, 491 U.S. 781, 799 (1989).

[4] The horizontal ownership limit restricts "the number of cable subscribers" any commonly-owned cable systems are "authorized to reach." The vertical limit restricts "the number of channels on a cable system that can be occupied" by integrated programming suppliers (*i.e.*, those in which cable operators have ownership interests). 47 U.S.C. § 533(f)(1)(A) & (B).

[5] *See also Chesapeake and Potomac Telephone Company of Virginia v. United States*, 42 F.3d 181 (4th Cir. 1994); *US West, Inc. v. United States*, 48 F.3d 1092 (9th Cir. 1994) (applying intermediate scrutiny to a market structure regulation prohibiting telephone companies from providing video programming to subscribers within their service areas).

have failed to consider the practical, legal and policy implications of routinely subjecting economic regulations to heightened constitutional scrutiny.

Amicus believes that reflexively subjecting the economic regulation of a specific communications-related industry, such as cable, to heightened judicial review gives insufficient consideration to the policy judgments of Congress, and is not required by this Court's previous decisions or the First Amendment. Obviously, if regulations analogous to the horizontal and vertical ownership limits at issue in this case were imposed on a particular non-communications industry, they would receive only a rational basis review and would be upheld if they bore a "reasonable relation" to a "legitimate" governmental "purpose." [6]

Indeed, the trend in the courts of appeals to subject structural regulation of communications entities to heightened First Amendment scrutiny is in considerable tension, if not outright conflict with, this Court's precedents. This Court has made clear that a regulation is not subject to heightened

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[6] *Exxon Corporation v. Governor of Maryland,* 437 U.S. 117, 124-25 (1978) (applying rational basis review to a state law prohibiting oil producers and refiners from operating their own retail service stations, which was enacted because the state believed that "producers and refiners were favoring company-operated stations in the allocation of gasoline and that this would eventually decrease the competitiveness of the retail market"). Similarly, Congress directed the FCC to establish the vertical and horizontal ownership restrictions at issue here "to enhance effective competition" because it believed that (i) "cable operators affiliated with video programmers" would "favor such programmers in determining carriage on their cable systems" or "restrict the flow of the video programming of such programmers to other video distributors," and (ii) cable operators because of their "size" could "unfairly impede" the "flow of video programming" to the "consumer." 47 U.S.C. §§ 533(f)(1), (f)(2)(A) & (f)(2)(B). *Amicus* challenges the cable industry's position that Congress' discretion to adopt industry-specific economic regulations automatically lessens if the industry in question is communications-related.

review merely because it affects a communications-related industry, unless there is "an additional basis for concluding" that such a regulation was adopted for a speech-repressive or other invidious purpose. *Leathers v. Medlock*, 499 U.S. 439, 449 (1991). To the contrary, economic regulation of a communications or speech-related industry does not raise any issue warranting heightened scrutiny, even if a "differential burden" is placed on different types of media,[7] unless the regulation was in fact directed at, or intended to impact, protected speech. *See Leathers*, 499 U.S. at 453 (the "differential taxation of speakers, even members of the press, *does not implicate the First Amendment* unless the tax is directed at, or presents the danger of suppressing, particular ideas") (emphasis added).[8]

Leathers clearly undercuts the assumption that virtually any type of economic regulation specifically affecting the cable industry automatically merits heightened judicial scrutiny. Certainly this Court has previously rejected relying on the First Amendment as a basis for reviewing economic regulations, even in cases directly involving speech or other First Amendment-related activities. For example, in *Regan v. Taxation with Representation of Washington*, 461 U.S. 540 (1983), this Court upheld, under a rational basis review, a tax statute that treated certain nonprofit organizations more

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[7] *Leathers*, 499 U.S. at 452 (the extension of an existing sales tax to cable television service, while continuing to exempt print media, held not to violate First Amendment). *See also R.A.V. v. City of St. Paul, Minnesota*, 505 U.S. 377, 387-88 (1992) (in examining the constitutionality of a city hate speech ordinance, the Court observed that the State could prohibit obscenity "only in certain media or markets" and could "choose to regulate price advertising in one industry but not in others").

[8] *See also Lorain Journal Co. v. United States*, 342 U.S. 143 (1951) (the application of the anti-trust laws to a newspaper that attempted to force its advertisers to boycott a competing radio station was held not to violate the First Amendment, even though the newspaper publisher claimed a right to select its customers and to refuse to accept advertisements from whomever it pleased).

favorably if they did not engage in substantial lobbying activities. The court of appeals in *Regan* had determined that heightened scrutiny was required because the statute "affect[ed] First Amendment rights on a discriminatory basis." *Taxation With Representation of Washington v. Regan*, 676 F.2d 715, 728 (D.C. Cir. 1982). This Court rejected that reasoning, and concluded that the tax statute did not violate either the First or Fifth Amendment rights of the appellant nonprofit organization. The Court found, in particular, "no indication that the statute was *intended to suppress any ideas* or any demonstration that it has had that effect." *Regan*, 461 U.S. at 548 (emphasis added).

Amicus accordingly asserts that an economic regulation applicable to an industry engaged in speech-related activities, such as cable, should not be subjected to heightened scrutiny absent any "indication that the statute was intended" to, or had the effect of, "suppress[ing] any ideas." *Id.* This Court has, in fact, previously applied rational basis review in a case challenging on constitutional grounds a provision of the 1984 Cable Act that required local cable franchising of certain Satellite Master Antenna Television (SMATV) facilities. *FCC v. Beach Communications, Inc.*, 508 U.S. 307 (1993). Although the SMATV operators in *Beach* contended that the FCC had construed the 1984 Cable Act in a manner violating the equal protection component of the Fifth Amendment by not requiring the franchising of similar SMATV facilities, this Court upheld the Act under a rational basis review because in the "areas of social and economic policy," it is not for the "courts to judge the wisdom, fairness, or logic of legislative choices." *Beach*, 508 U.S. at 313. Surely the standard of review applied in *Beach* should not have differed if First Amendment claims, as well as equal protection claims, had been considered.[9] Yet under the logic of the

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[9] This Court has in fact expressed clear skepticism about relying "on the First Amendment" to review "economic regulations," and has asserted

court of appeals decision in the present case, such heightened scrutiny would have been warranted in *Beach*.

In sum, a number of decisions by this Court cast doubt on the cable industry's position that structural or other economic regulations affecting it automatically merit heightened First Amendment scrutiny. This Court's decisions in the *Turner* cases are not to the contrary.[10] In these cases, this Court applied intermediate scrutiny to rules requiring most cable systems to set aside up to one-third of their channels for the carriage of local commercial broadcast signals. 47 U.S.C. § 534(b)(1)(B). This set-aside requirement "reduce[d] the number of channels over which cable operators exercise[d] unfettered control," and the cable industry complained that the requirement "render[ed] it more difficult for cable programmers to compete for carriage on the limited channels remaining." *Turner I*, 512 U.S. at 636-37. The cable operators also claimed in *Turner I* that, as a consequence of the broadcast carriage requirements, "some cable programmers who would have secured carriage in the absence of must-carry may now be dropped." *Id.* at 657.[11]

Thus, the must carry rules at issue in the *Turner* cases directly regulated the speech of cable system operators—and were claimed to directly foreclose speech opportunities for some cable programmers—by requiring carriage of certain broadcast programming. Indeed, the cable system operators in *Turner I* contended that the must carry provisions should

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that "economic regulation . . . should enjoy the same strong presumption of validity that we accord to other policy judgments made by Congress." *Glickman v. Wileman Brothers & Elliott, Inc.*, 521 U.S. 457, 476-77 (1997).

[10] *Turner Broadcasting System, Inc. v. FCC*, 512 U.S. 622 (1994) (*Turner I*); *Turner Broadcasting System, Inc. v. FCC*, 520 U.S. 180 (1997) (*Turner II*).

[11] On remand, the cable industry was unable to substantiate this latter claim.

"trigger strict scrutiny because they *compel* cable operators to transmit speech not of their choosing." 512 U.S. at 653 (emphasis added).[12] Because the must carry rules directly regulate speech for other, non-content related purposes, this Court properly applied intermediate scrutiny in *Turner*.

In contrast, structural or other economic regulations applicable to the cable industry, including the ownership limits at issue here, do not regulate speech, compel speech, or even affect speech directly. It is, for example, difficult to discern how certain economic regulations (such as cable rate regulation) even remotely burden speech. The horizontal and vertical limits similarly do not directly impact *speech*, but regulate the ownership and economic structure of the cable industry. A legislative or regulatory determination that a single entity should not reach more than a certain percentage of a market, or otherwise exercise excessive control in a market through its integrated ownership interests, is not a regulation of *speech* meriting heightened judicial scrutiny, even if the "market" at issue is for video programming.[13] Nor

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[12] This Court has explicitly determined that the First Amendment is implicated when the government attempts to compel expression. *See, e.g., Pacific Gas and Elec. Co. v. Public Utilities Commission of California*, 475 U.S. 1 (1986). However, in *Turner I*, the Court rejected the application of strict scrutiny because the must carry rules were content neutral, and would not "force cable operators to alter their own messages to respond to the broadcast programming they are required to carry." 512 U.S. at 655. The Court also emphasized that the First Amendment did not "disable" the government from ensuring that cable system operators did "not restrict, through physical control of a critical pathway of communication, the free flow of information" into subscribers' homes. *Id.* at 657.

[13] This Court has previously upheld against First Amendment challenges FCC rules similarly regulating the ownership and structure of the broadcast industry without engaging in any heightened scrutiny. *See, e.g., FCC v. NCCB*, 436 U.S. 775 (1978) (upholding the prohibition on common ownership of a daily newspaper and a broadcast facility in the same geographic market).

has there ever been a suggestion that the cable ownership limits were intended to prevent any speaker's ideas from becoming too powerful, but rather were motivated by unexceptional concerns about the cable industry's economic dominance and preserving competition in the video programming market.

It is thus a misreading of the *Turner* decisions to conclude that they stand for the proposition that all economic or structural regulations affecting the cable industry merit increased scrutiny by reviewing courts. The courts of appeals have consequently erred by interpreting *Turner* as requiring the application of heightened scrutiny in all cases involving regulation of the cable industry, even if the regulation in question may not actually regulate or burden speech. *See Time Warner*, 56 F.3d at 185 (D.C. Circuit applied intermediate scrutiny to FCC's cable rate regulations, even though it was "by no means clear how" rules "requiring cable operators to charge reasonable rates burden speech"). Given the frequency with which Congress adopts legislation affecting the cable and other telecommunications industries, these questions will no doubt continue to arise in numerous cases. Review should accordingly be granted to provide much needed clarity respecting the standard of review applicable to structural economic regulation of communications industries.

C. The Oral Argument Before This Court In A Case Following *Turner I* Reveals Unresolved Questions Pertaining To The Appropriate Level Of Review Of Economic Regulations Affecting Communications-Related Industries.

Members of this Court also clearly expressed reservations about applying a heightened level of First Amendment scrutiny to the economic regulation of a communications-related industry in oral argument in cases involving the now-eliminated statutory restrictions on local telephone companies providing video programming to subscribers within their

service areas. *See* Transcript of Oral Argument in *United States v. Chesapeake and Potomac Telephone Company of Virginia; NCTA, Inc. v. Bell Atlantic Corp.*, Nos. 94-1893, 94-1900, 1995 U.S. Trans Lexis 107 (Dec. 6, 1995).[14] Significantly, this uncertainty about the appropriate "standard of review" (*id.* at *30) to apply toward an economic/structural regulation restricting telephone companies from providing video programming was expressed *after* the decision in *Turner I*.

As observed in the *Chesapeake and Potomac* oral argument, "what we have here really is classical economic regulation" that "happens to be economic regulation in an area where people are providing . . . communication services." 1995 U.S. Trans Lexis 107 at *30. Because the government's interest in this case was "an economic one," *id.* at *33, questions were raised about "retreat[ing] from giving Congress quite a lot of discretion when it tries to deal with the structure of industries," and about the grounds for "depart[ing] from the normal rational basis" when "dealing with economic regulation in the communications area." *Id.* at *30-31.

As also noted in this oral argument, the United States is "becom[ing] more and more a speech-intensive, speech-creative, speech-obsessed society," and concern was expressed about "hav[ing] more and more cases" involving First Amendment challenges to economic regulations as others, such as "software manufacturer[s]," assert that they are "engaged in speech." *Id.* at *32. The questions posed additionally reveal concern by this Court that Congress should be able to pass "an economic regulation" (such as one "to protect consumers . . . from prices") that applies to a

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[14] The Court never issued an opinion in these cases because they were mooted by passage of the 1996 Telecommunications Act, which eliminated the challenged restrictions (formerly contained in 47 U.S.C. § 533(b)) on telephone companies.

communications-related industry (such as "the broadcast cable industry"), rather than "cement companies," because "[t]hat's what [Congress is] interested in." *Id.* at *37-38.[15] In sum, the *Chesapeake and Potomac* oral argument raised the question of whether "this whole big economic area" of regulating communications services would "be turned over to courts." *Id.* at *30.

From the lengthy discussion in *Chesapeake and Potomac*, the members of this Court evidently do not regard *Turner* as having resolved all questions concerning the appropriate level of scrutiny for reviewing structural or other economic regulations affecting communications industries. *Amicus* urges the Court to grant CFA's petition for certiorari to address these issues specifically, and resolve the questions about the grounds for "depart[ing] from the normal rational basis" review when "dealing with economic regulation in the communications area." Oral Argument in *Chesapeake and Potomac*, 1995 U.S. Trans Lexis 107 at *31.

As communications-related industries become an ever larger and more important part of the U.S. economy, questions concerning the discretion of Congress and the states to regulate the ownership and structure of these industries will only proliferate. *See* 1995 U.S. Trans Lexis 107 at *32. But the insistence of the cable industry that any structural or economic regulation affecting it automatically requires heightened First Amendment scrutiny harkens back to the (now discredited) jurisprudence limiting the government's economic regulatory policies under the due process clause. *See, e.g., Lochner v. New York*, 198 U.S. 45 (1905). This

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[15] Members of this Court further specifically inquired as to why Congress could not enact "a statute parallel to the banking regulation" . . . to prevent telephone companies from "tak[ing] undue risks with their capital" by engaging in the provision of video programming or "any business except what they do now." *Id.* at *34.

Court clearly rejected such constitutional limits on Congress' and the states' regulatory authority decades ago.[16]

There would, moreover, seem to be no discernible limit to the position espoused by the cable industry, as innumerable governmental regulatory initiatives may, to varying degrees, involve speech or speech-related conduct. This Court's First Amendment jurisprudence has "not left Congress or the States powerless to address" serious economic or societal problems, and should not be interpreted as "imposing" rigid "judicial formulas" that "disable[] government from responding to serious problems." *Denver Area Educational Telecommunications Consortium, Inc. v. FCC*, 518 U.S. 727, 740-41 (1996) (plurality opinion).[17] Indeed, this Court has expressly recognized that regulatory policies promoting economic competition are congruent with—rather than contrary to—the First Amendment because they promote diverse sources of speech.[18]

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[16] *See, e.g., United States v. Carolene Products Co.*, 304 U.S. 144 (1938). *See also Chesapeake and Potomac* Oral Argument, 1995 U.S. Trans Lexis 107 at *30 (questioning the use of the First Amendment to "retreat from giving Congress quite a lot of discretion when it tries to deal with the structure of industries," and noting that "other people in history have used other amendments to sort of go into economic regulation in great depth").

[17] *See also CBS, Inc. v. DNC*, 412 U.S. 94, 102-3 (1973) ("'[W]e must construe [the First Amendment] as part of a Constitution which creates a government for the purpose of performing several very important tasks. The (First) Amendment should be interpreted so as not to cripple the regular work of the government. A part of this work is the *regulation of interstate and foreign commerce* . . . . '") (*quoting* 2 Z. Chafee, *Government and Mass Communications* 640-641 (1947)) (emphasis added).

[18] *See, e.g., Associated Press v. United States*, 326 U.S. 1, 20 (1945) (concluding that the "First Amendment, far from providing an argument against application" of the antitrust laws to the press, "provides powerful reasons to the contrary," as "[t]hat Amendment rests on the assumption

To ensure appropriate consideration to legislative policy judgments, the courts should accordingly afford Congress equal discretion to pass "an economic regulation" that "protect[s] consumers" from unreasonable "prices, or whatever," whether such regulation applies to a communications industry or to "cement companies," 1995 U.S. Trans Lexis 107 at *37-38, unless the regulation applicable to a communications industry "is directed at, or presents the danger of suppressing, particular ideas." *Leathers*, 499 U.S. at 453.[19] Certainly the appellate courts' almost reflexive application of heightened First Amendment scrutiny to any structural or economic regulation of the cable or other communications industry does not appear warranted.[20] Even counsel representing the telephone companies in the *Chesapeake and Potomac* cases, when questioned about the level of scrutiny to be applied, admitted that "[r]ules about the *structure* of an industry, about who may *own* what, are really quite different" [than the challenged ban on providing video programming]. 1995 U.S. Trans Lexis 107 at *31 (emphasis added). Because the record in this case contains no indication whatsoever that the horizontal and vertical cable ownership rules were "intended to suppress any ideas" or have "had that effect," *Regan*, 461 U.S. at 548, the court of appeals erred in concluding, under a heightened level of review, that the FCC had not met its burden of justifying these regulations under the First

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that the widest possible dissemination of information from diverse and antagonistic sources is essential to the welfare of the public").

[19] *See also Associated Press*, 326 U.S. at 7 (court observed that publishers "are engaged in business for profit exactly as are other business men who sell food, steel, aluminum, or anything else people need or want . . . .The fact that the publisher handles news while others handle food does not . . . afford the publisher a peculiar constitutional sanctuary" from application of antitrust regulation).

[20] *See, e.g., FCC v. Beach*, 508 U.S. at 313 (in the area of "economic policy," it is not for the "courts to judge the wisdom, fairness, or logic of legislative choices").

Amendment.[21] This Court should therefore grant the petition for writ of certiorari in this proceeding.

II. THIS COURT SHOULD GRANT REVIEW TO CLARIFY THE LEVEL OF DEFERENCE THAT REVIEWING COURTS SHOULD ACCORD BOTH TO STATUTORY PROVISIONS AND TO AGENCY RULES PROMULGATED UNDER A SPECIFIC GRANT OF STATUTORY AUTHORITY.

As noted in CFA's petition (at 26), the cable ownership regulations were not adopted under the Commission's generic statutory powers, but were "issued under a specific grant of authority to . . . prescribe a method of executing a statutory provision." *Rowan Cos., Inc. v. United States*, 452 U.S. 247, 253 (1981).[22] The court of appeals should accordingly have shown greater deference to the FCC's interpretation of Section 533(f) than to any regulation adopted pursuant to the FCC's general authority under the 1934 Communications Act to regulate in the "public interest, convenience, and necessity."[23] Indeed, the horizontal and vertical ownership

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[21] *Compare R.A.V.*, 505 U.S. at 394 (in holding unconstitutional a city hate speech ordinance, the Court expressly found that the city's intent in adopting the ordinance was to "handicap the expression of particular ideas").

[22] Specifically, Congress directed the FCC "to prescribe rules and regulations establishing *reasonable* limits" on the reach of commonly-owned cable systems and on cable operators' integrated ownership interests in programmers. 47 U.S.C. § 533(f)(1)(A) & (B) (emphasis added). The word "reasonable" is "among the broadest in the congressional lexicon of delegation." *Williams Natural Gas Co. v. FERC*, 943 F.2d 1320, 1331 (D.C. Cir. 1991).

[23] *See Rowan*, 452 U.S. at 253; *United States v. Vogel Fertilizer Co.*, 455 U.S. 16, 24 (1982) (reviewing court owes less deference to a regulation promulgated under an agency's general authority to "prescribe all needful rules" than to a regulation "issued under a specific grant of

limits should have—and clearly did not—receive "more than mere deference or weight."[24] In Section 533(f), Congress "expressly *delegated*" to the Commission "the power to prescribe" rules and regulations establishing the cable ownership limits at issue here. *Batterton*, 432 U.S. at 425 (emphasis in original). "In a situation of this kind, Congress entrusts" to the Commission, "rather than to the courts, the primary responsibility for interpreting the statutory term[s]," and a "reviewing court is not free to set aside those regulations," which have "legislative effect," even though "it would have interpreted the statute in a different manner." *Id.*

But instead of showing "controlling" weight to the Commission's legislative rules implementing Section 533(f),[25] the court of appeals in this proceeding showed so little deference that it effectively undermined Congress' clear intent in passing this section and expressly delegating authority for its implementation to the Commission. Such decisions frustrate the ability of Congress to rely on administrative agencies, and pressure Congress to, in effect, write regulations as statutes so as to obtain proper deference to its wishes from the judiciary. The cumulative result of decisions such as the appellate court's here would be to prevent Congress from relying on the experience and expertise of agencies in formulating regulatory policies, and, ultimately, to cause a decline in the quality of regulatory decisions.[26]

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authority to define a statutory term or prescribe a method of executing a statutory provision").

[24] *Batterton, Secretary, Department of Human Resources of Maryland v. Francis*, 432 U.S. 416, 426 (1977) (upholding agency's prescription of standards under a provision of the Social Security Act).

[25] *United States v. O'Hagan*, 521 U.S. 642, 673 (1997) (Court owed "controlling weight" to legislative rules prescribed by agency).

[26] For these reasons, numerous cases emphasize the importance of courts deferring to the expertise and predictive judgments of agencies. *See, e.g., Pauley v. Bethenergy Mines, Inc.*, 501 U.S. 680, 697 (1991)

But even beyond the deference owed to agencies when adopting legislative rules, this Court has stressed the significant deference owed by the judiciary to the judgments of Congress. *See, e.g., Turner II*, 520 U.S. at 195-96. Reviewing courts should therefore not be able to circumvent the deference they owe to Congress by first upholding a challenged statute under deferential review, but then showing virtually no deference to the regulations promulgated by the agency expressly directed to implement the same statute.[27]

An instructive comparison can be made between the case initially upholding the constitutionality of the statutory provisions directing the Commission to establish the horizontal and vertical ownership limits, and the later decision striking down the FCC's regulations implementing those provisions. In the first decision, the court easily upheld Section 533(f), clearly giving deference to "Congress's predictive judgments" and dismissing assertions that Congress acted without sufficient evidence and findings. *Time Warner Entertainment Co., L.P. v. United States*, 211 F.3d 1313, 1319-20, 1322 (D.C. Cir. 2000).[28] In complete contrast, when examining the

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(deference to agency was "appropriate" because the "regulatory program" at issue was "complex and highly technical," requiring "significant expertise" and the "exercise of judgment grounded in policy concerns"); *NCCB*, 436 U.S. at 813-14 (this Court reversed lower court for failing to show proper deference to determinations of FCC that "were primarily of a judgmental or predictive nature"). Even in evaluating "First Amendment claims," this Court has emphasized that "we must afford great weight to the decisions of Congress and the experience of the Commission." *CBS*, 412 U.S. at 102.

[27] *See Williams Natural Gas*, 943 F.2d at 1332 (court rejected challenges to an agency decision concerning price ceilings for natural gas, saying "[i]t is not our office to argue energy policy with the legislature, *nor a fortiori with the agency it has charged with implementing that policy*") (emphasis added).

[28] For example, although the court could not say, on the evidence presented, that the horizontal "ownership cap will surely increase the

FCC's rules, the court engaged in "an intermediate in theory, but strict in fact" review (CFA's petition at 23) that showed little or no deference to the Commission.[29]

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diversity of programming," it was "enough" that "Congress reasonably concluded" that greater concentration in the cable industry "threatened the diversity of information available to the public." *Time Warner*, 211 F.3d at 1320. Similarly, complaints that the vertical ownership limit addressed "only a speculative harm" were rejected with a brief reference to congressional findings on the issue, and the comment that Congress' concern was grounded in "a bit of economic common sense." *Id.* at 1322.

[29] For instance, from the outset, the court stressed that its review of the regulations (as opposed to the earlier review of the statutory provisions) presented an "independent set of questions," and that, just because there was "authority to impose some [ownership] limit," the Commission did not have "authority to impose any limit imaginable." *Time Warner*, 240 F.3d at 1129-30. The court consistently dismissed both Congress' and the Commission's findings as conjectural and/or insufficient to support the regulations, although Congress' findings had easily been found sufficient to justify the statutory provisions. *Id.* at 1130-32; 1137. (Particularly puzzling in this regard is the court's conclusion that both Congress and the FCC failed to provide sufficient support to justify the horizontal ownership limit as protective of potential programmers from joint cable operator action. After all, the statute expressly directed the FCC to "ensure" that no "group of cable operators" could "unfairly impede" because of "joint actions" the flow of video programming to consumers. 47 U.S.C. § 533(f)(2)(A).) With regard to questions of economic and competition policy, the court second-guessed the FCC's judgment on a number of points (*see* 240 F.3d at 1132-35) and, in one instance, dismissed the FCC as offering only an "economic commonplace." *Id.* at 1132. *Compare Time Warner*, 211 F.3d at 1322 (upholding vertical ownership statutory restriction because Congress' concern was grounded in "economic common sense"). Most seriously, the court clearly substituted its own judgment for the judgment of the FCC, especially with regard to the appropriate level of the horizontal ownership limit. *See Time Warner*, 240 F.3d at 1132 (indicating that a horizontal limit of 60% was justified, rather than the FCC's 30% limit) and 1136 (asserting that Section 533(f) greatly confined the FCC's authority to regulate in its long-standing interest of diversity, even though the statute did not say so and, in fact, directed the FCC to take into account specifically enumerated diversity-related concerns, as well as "other public interest objectives").

This stark difference between the level of deference afforded the cable ownership statutory provisions and the cable ownership rules simply cannot be justified. At the very least, the review accorded legislative rules adopted by agencies pursuant to express statutory directives should not be so strict as to thwart congressional intent and undermine the significant deference that reviewing courts owe to Congress. *See Chevron U.S.A. Inc. v. NRDC, Inc.*, 467 U.S. 837, 865-66 (1984) (stressing that Congress and executive branch agencies, which are politically accountable, should make "policy choices," and that "federal judges—who have no constituency—have a duty to respect legitimate policy choices made by those who do"). Given the court of appeals' ultimate failure to give proper deference to Congress' judgment concerning the ownership structure of the cable industry, this Court should grant CFA's petition for certiorari.

CONCLUSION

For the foregoing reasons, the National Association of Broadcasters urges the Court to grant the petition for certiorari in this case to address issues significantly affecting Congress' economic regulatory powers and the ability of administrative agencies to implement explicit congressional directives.

Respectfully submitted,

HENRY L. BAUMAN
JACK N. GOODMAN *
JERIANNE TIMMERMAN
NATIONAL ASSOCIATION OF BROADCASTERS
1771 N Street, N.W.
Washington, D.C. 20036
(202) 429-5430

* Counsel of Record

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